2010

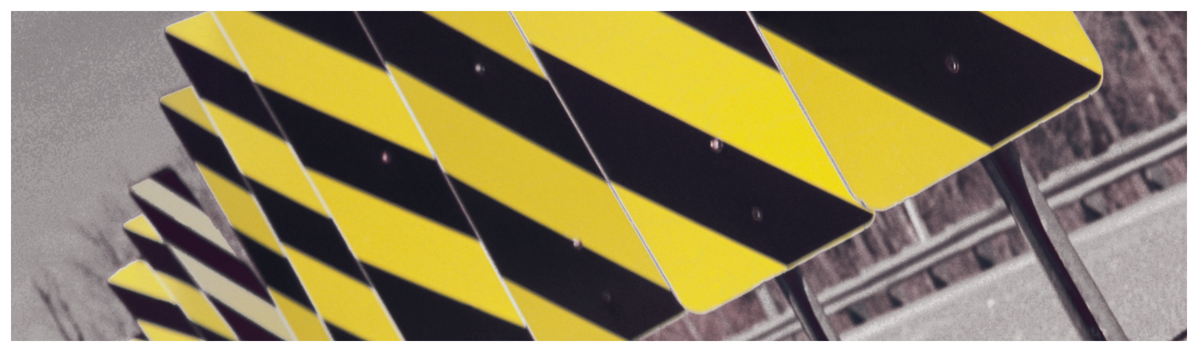
Health care industry developments - 2010/11; Audit risk alerts

American Institute of Certified Public Accountants (AICPA)

2010/11

Health Care Industry Developments

AUDIT RISK ALERT



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Audit Risk Alert: 2010/11 Health Care Industry Developments

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Health Care Industry Developments

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Notice to Readers

This Audit Risk Alert replaces *Health Care Industry Developments—2009*.

This Audit Risk Alert is intended to provide auditors of financial statements of health care entities with an overview of recent economic, industry, technical, regulatory, and professional developments that may affect the audits and other engagements they perform. This Audit Risk Alert also can be used by an entity's internal management to address areas of audit concern.

This publication is an *other auditing publication*, as defined in AU section 150, *Generally Accepted Auditing Standards* (AICPA, *Professional Standards*, vol. 1). Other auditing publications have no authoritative status; however, they may help the auditor understand and apply the Statements on Auditing Standards.

If an auditor applies the auditing guidance included in an other auditing publication, he or she should be satisfied that, in his or her judgment, it is both relevant to the circumstances of the audit and appropriate. The auditing guidance in this document has been reviewed by the AICPA Audit and Attest Standards staff and published by the AICPA and is presumed to be appropriate. This document has not been approved, disapproved, or otherwise acted on by a senior technical committee of the AICPA.

Recognition

The AICPA gratefully appreciates the invaluable assistance Anne Mundinger provided in creating this publication.

The AICPA gratefully acknowledges the following individuals for their essential contributions in creating this publication:

Mark Albrecht
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Feedback

The Audit Risk Alert *Health Care Industry Developments* is published annually. As you encounter audit or industry issues that you believe warrant discussion in next year's Audit Risk Alert, please feel free to share them with us. Any other comments that you have about the Audit Risk Alert also would be appreciated. You may e-mail these comments to A&A Publications@aicpa.org.

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How This Alert Helps You

.01 This Audit Risk Alert (alert) helps you plan and perform your health care industry audits and also can be used by an entity's internal management. This alert provides information to assist you in achieving a more robust understanding of the business, economic, and regulatory environments in which your clients operate. This alert is an important tool to help you identify the significant risks that may result in the material misstatement of financial statements and delivers information about emerging practice issues and current accounting, auditing, and regulatory developments. You should refer to the full text of accounting and auditing pronouncements, as well as the full text of any rules or publications that are discussed in this alert. Additionally, the Audit Risk Alert *General Accounting and Auditing Developments—2010/11* (product no. 0223310) explains important issues that affect all entities in all industries in the current economic climate.

.02 It is essential that the auditor understand the meaning of audit risk and the interaction of audit risk with the objective of obtaining sufficient appropriate audit evidence. In AU section 312, *Audit Risk and Materiality in Conducting an Audit* (AICPA, *Professional Standards*, vol. 1), *audit risk* is broadly defined as the risk that the auditor may unknowingly fail to appropriately modify his or her opinion on financial statements that are materially misstated. Further, paragraph .04 of AU section 314, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement* (AICPA, *Professional Standards*, vol. 1), explains that the auditor should use professional judgment to determine the extent of the understanding required of the entity and its environment. The auditor's primary consideration is whether the understanding that has been obtained is sufficient to assess risks of material misstatement of the financial statements and to design and perform further audit procedures.

Economic and Industry Developments

The Current Economy

.03 When planning and performing audit engagements, an auditor should understand both the general current economy and the specific economic conditions facing the industry in which the client operates. Economic activities relating to factors such as interest rates, availability of credit, consumer confidence, overall economic expansion or contraction, inflation, and labor market conditions are likely to have an effect on an entity's business and, therefore, its financial statements.

.04 The year 2010 may be the beginning of a wave of economic recovery. Although many key indicators, such as unemployment, are still uncomfortably high, 2010 began with rising commodity prices, a jump in new factory orders that caused the largest expansion in production in 3 years, and an increase in U.S. auto sales that approached prerecessionary levels. Further, after experiencing a considerable decline in the stock market through March 2009, the markets have rebounded substantially. In March 2009, the S&P 500 and the Dow Jones Industrial Average reached their 12-year lows, and NASDAQ closed at its lowest point since October 2002. By March 2010, only a year later, all 3 had increased in value by at least 59 percent from the previous year's lows.

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However, all 3 remained relatively unmoved 6 months later, in late September 2010. This exhibits the continuing uncertainty in the markets due to the varying economic indicators, the financial reform regulatory changes, and Europe's economy, among other reasons.

Key Economic Indicators

.05 These key economic indicators further illustrate the severity of the recent recessionary period experienced by the United States.

.06 The gross domestic product (GDP) measures output of goods and services by labor and property within the United States. It increases as the economy grows or decreases as it slows. According to the Bureau of Economic Analysis, real GDP increased at an annual rate of 1.6 percent in the second quarter of 2010 (second estimate), 3.7 percent in the first quarter of 2010, and 5.6 percent in the fourth quarter of 2009. This data indicates a turnaround in the economy because in the fourth quarter of 2008 and the first quarter of 2009, real GDP decreased 6.3 percent and 5.5 percent, respectively. Further, in June 2010, the Treasury reported that banks had repaid about 75 percent of the bailout money they received through the Troubled Asset Relief Program, and that taxpayers made $21 billion on the investment. However, other bailouts are not yet repaid, and they may yield losses to taxpayers.

.07 From August 2009 to August 2010, the unemployment rate fluctuated between 9.5 percent and 10.1 percent. An unemployment rate of 10.0 percent represents approximately 15.3 million people. The annual average rate of unemployment increased from 4.6 percent in 2007 to 9.3 percent in 2009. However, through August 2010, the rate has remained below 10.0 percent.

.08 The Federal Reserve decreased the target for the federal funds rate more than 5.0 percentage points to less than 0.25 percent, where it remained through September 2010. The Federal Reserve described the current economic recovery in its September 21, 2010, press release as follows:

- Household spending is increasing gradually but remains constrained by high unemployment, modest income growth, lower housing wealth, and tight credit.
- Business spending on equipment and software is rising, though less rapidly than earlier in the year, and investment in nonresidential structures continues to be weak.
- Employers remain reluctant to add to payrolls.
- Housing starts are at a depressed level.
- Bank lending has continued to contract, but at a reduced rate in recent months.
- The pace of economic recovery is likely to be modest in the near term.

.09 The Federal Reserve also noted in the press release that "economic conditions, including low rates of resource utilization, subdued inflation trends, and stable inflation expectations, are likely to warrant exceptionally low levels of the federal funds rate for an extended period." The Federal Reserve will keep constant their holdings of securities by reinvesting principal payments from mortgage-backed securities in longer-term Treasury securities; additionally, as current holdings of Treasury securities mature, the proceeds will be reinvested in Treasury securities. Since the beginning of the financial market turmoil in

August 2007, the Federal Reserve's balance sheet has grown from $869 billion to $2.3 trillion. Further, the Federal Reserve will continue to monitor the economy and employ other policy tools as necessary.

Industry Trends and Conditions

The State of Health Care Entities

.10 A survey conducted by the American Hospital Association (AHA) in March and April 2010 indicated that hospitals are continuing to feel the lingering effects of the economic recession. The survey of 572 nonfederal, short-term acute care hospitals shows the following:

- Eighty-seven percent reported increased bad debt and charity care as a percentage of total gross revenue, and 65 percent reported an increased percentage of patients covered by Medicaid, Children's Health Insurance Program, or other programs.
- Seventy-two percent reported depressed numbers of elective procedures, and 70 percent reported depressed overall patient volumes.
- Seventy-four percent reported reduced operating margins, and 50 percent reported reduced nonoperating income.
- In 2009, in an effort to weather the economic storm, 76 percent had cut administrative costs, 73 percent delayed capital investments, and 53 percent reduced staff. In 2010, 98 percent have not restored services or programs, 89 percent have not added back staff or increased hours, and 67 percent have not started or continued capital projects.

.11 More information about the AHA and the full survey results are available at www.aha.org.

Medical Liability Reform

.12 Hospitals and physicians continue to deal with increasing costs for professional liability insurance. Unaffordable insurance costs are affecting access to care as physicians leave states with high costs or stop providing services that expose them to higher risks of lawsuits. Obstetrics, neurosurgery, and emergency services are some of the areas of highest concern. Physicians concerned with increasing risk often practice "defensive medicine," which is the practice of providing extra care to minimize lawsuits. The Patient Protection and Affordable Care Act of 2010 (PPACA) appropriated $50 million for demonstration projects that test models aimed at reducing frivolous lawsuits and liability premiums. Medical liability reform is expected to reduce federal mandatory spending on health programs by $41 billion dollars over the next 10 years. Due to the fact that this is generally an area of significant estimates, entities and their auditors need to understand and test liability claims estimates. Assumptions and judgments employed by management should be carefully reviewed and should reflect current environment issues. Auditors need to consider all available remedies for supporting estimates, including the entity's historical experience, attorney confirmations, and available correspondence.

Physician Practice Acquisitions

.13 Industry analysts expect to see a rise in merger and acquisition activity due to the pressures on health care payers and providers brought about by the PPACA. Faced with increased patient volumes at lower levels of reimbursement, more and more physicians are aligning their practices with a hospital or health system.

.14 A major trend exists in cardiology, medical oncology, and many other areas of physician practice acquisitions by hospitals driven by physicians facing reimbursement cuts, as well as difficulty in recruiting young physicians. In many of these transactions, after identification of all intangible assets, a significant amount of goodwill is often recorded by the acquirer. Recording goodwill from such transactions may have a high probability of impairment when the intangible asset values of the practice are based solely on the cost approach to valuation. Acquiring entities and their auditors should carefully review the methodology used to value the physician practices being acquired. Forecasts used to support the valuation assessments need to be reviewed carefully.

.15 New accounting guidance requires not-for-profit (NFP) organizations to test goodwill for impairment at the beginning of the year and at least once annually. Entities have a six month initial application period to complete the first step of a transitional impairment. Evaluation and impairment resulting from this testing is recorded "below the line" as the effect of a change in accounting principle. The transitional evaluation must be completed by the end of the fiscal year of adoption.

.16 Fee-for-service NFPs with previously recognized goodwill will need to

a. establish reporting units based on the entity's internal reporting structure.

b. assign all previously recognized goodwill in each reporting unit as of the beginning of the fiscal year to a transitional impairment evaluation.

c. subject the previously recognized goodwill in each reporting unit as of the beginning of the fiscal year to a transitional impairment evaluation.

d. if the carrying amount of a reporting unit's net assets, including goodwill, exceeds the fair value of that reporting unit, complete the second step of the transitional goodwill impairment test as soon as possible but no later than the end of the fiscal year.

e. reassess useful lives of any previously recognized intangible assets, other than goodwill, and adjust the remaining amortization periods as necessary. The reassessment should be completed before the end of the first interim period of the fiscal year in which the statement is initially applied. Intangible assets deemed to have indefinite useful lives should be tested, and any resulting impairment should be accounted for in the same manner as the procedures outlined for goodwill.

.17 In January 2010, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2010-07, *Not-for-Profit Entities (Topic 958): Not-for-Profit Entities: Mergers and Acquisitions*, which codifies FASB Statement No. 164, *Not-for-Profit Entities: Mergers and Acquisitions—Including an amendment of FASB Statement No. 142*, primarily in FASB

Accounting Standards Codification (ASC) 958-805 and FASB ASC 958-810. Readers are encouraged to review the full text of FASB Statement No. 164 and ASU No. 2010-07, which are available on the FASB website at www.fasb.org.

Provider Taxes

.18 States have attempted to increase the amount of federal matching funds for which they are eligible by increasing the amount of medical assistance they provide. In order to pay for the increased medical assistance, some states have imposed a tax on health care entities, sought donations or other voluntary payments from them, or both. As a result, the states have been able to generate additional federal matching funds without expending additional state funds.

.19 The accounting for these types of programs is dependent on the individual facts and circumstances. For example, if there is a guarantee that specific monies given to the state by the health care entity will be returned to the entity from the state, those amounts should be recorded as receivables. In addition, if the health care entity has met all the requirements to be legally entitled to additional funds from the state, the revenue or gain should be recognized.

.20 However, if the monies go into a pool with other contributions that are then disbursed based on factors over which the health care entity has little or no control, the payments should be recognized as an expense. Any subsequent reimbursements would be recognized as revenue or gain when the provider is entitled to them and payment is assured.

.21 Auditors should be alert to these issues, and management should be careful to avoid delayed recognition of expenses or improperly recognizing contingent gains.

Medical Resident Federal Insurance Contributions Act Refund Claims

.22 In March 2010, the IRS made an administrative determination to accept the position that medical residents are excepted from Federal Insurance Contributions Act (FICA) taxes for tax periods ending before April 1, 2005, when new IRS regulations went into effect. Although the period of limitations for filing a claim for tax periods before April 1, 2005, has expired, employers (typically hospitals and medical schools) and individual taxpayers (medical residents) began filing FICA refund claims in the 1990s, based on their position that medical residents are students eligible for the FICA tax exception under Internal Revenue Code (IRC) Section 3121(b)(10). This is referred to as the student exception and may apply to a student at a school, college, or university who is also an employee of that school, college, or university. The employer's FICA refund claims were for both the employer share and the employee share of the FICA tax. In some cases, individual medical residents filed their own claim for the employee share of the FICA tax. The IRS held the claims in suspense because there was a dispute about whether the student FICA exception applied.

Legislative and Regulatory Developments

The Health Care and Education Reconciliation Act of 2010 and the PPACA

.23 In March 2010, the president signed into law a sweeping overhaul of the health care system. Almost everyone in the United States will be affected by these changes—individuals, insurance companies, health care providers, and employers. The three primary goals of the reform are to expand coverage to those without health insurance, reform the delivery system of benefits to improve quality, and decrease the costs of providing health care. The various provisions of the reform will become effective over time, through 2020. The new laws contain many changes for employers to consider for financial reporting purposes, in addition to many new tax rules to help offset the overall cost of the reform.

.24 The complete changes are contained in two acts. The Health Care and Education Reconciliation Act of 2010 was signed on March 30 and is a reconciliation bill that amends the PPACA signed into law by the president one week earlier. In April, the Securities and Exchange Commission (SEC) issued a staff announcement, *Accounting for the Health Care and Education Reconciliation Act of 2010 and the Patient Protection and Affordable Care Act*, to address questions that have arisen about the effect, if any, that the different signing dates might have on accounting for the two acts. This timing difference, related solely to the signing dates, should not have an impact on a majority of registrants because the acts were both signed within a relatively short time period, which for the vast majority of entities, falls into the same reporting period. However, there may be a limited number of registrants with a period-end that falls between the signing dates for which the timing difference could raise questions about whether the different signing dates have an accounting impact.

.25 After consultation with FASB staff, the Office of the Chief Accountant would not object to a view that the two acts should be considered together for accounting purposes. That is, in this specific fact pattern, the SEC staff would not object to a registrant incorporating the effects of the Health Care and Education Reconciliation Act of 2010 when accounting for the PPACA. This view is based in part on the SEC staff's understanding that the two acts, when taken together, represent the current health care reform as passed by Congress and signed by the president. The SEC staff does not believe that it would be appropriate to analogize to this view in any other fact patterns.

Significant Accounting and Tax Considerations

.26 FASB ASC 740-10-30-2 states that the following basic requirements are applied to the measurement of current and deferred income taxes at the date of the financial statements:

- The measurement of current and deferred tax liabilities and assets is based on provisions of the enacted tax law; the effects of future changes in tax laws or rates are not anticipated.
- The measurement of deferred tax assets is reduced, if necessary, by the amount of any tax benefits that, based on available evidence, are not expected to be realized.

.27 FASB ASC 715-60-35-102 further explains that benefit coverage for medical claims by governmental programs or other providers of health care benefits should be assumed to continue as provided by the present law and other providers, pursuant to their present plans. Consistent with FASB ASC guidance, presently enacted changes in the law or amendments of the plans of other health care providers that take effect in future periods and that will affect the future level of their benefit coverage should be considered in current period measurements for benefits expected to be provided in those future periods. Future changes in laws concerning medical costs covered by governmental programs and future changes in the plans of other providers should not be anticipated.

.28 The two primary accounting considerations resulting from this reform are the effects of the tax law changes on deferred income tax balances and other postretirement health benefits. One of the most significant changes relates to the government subsidy for providing qualifying prescription drug coverage to Medicare-eligible retirees becoming an offset for prescription drug income tax deductions. Specifically, because entities will need to reduce their income tax deduction for providing prescription drug coverage by the subsidy received, they currently need to record a charge to earnings to write off a portion of their deferred tax assets related to postretirement health care obligations. Such deferred tax assets were based on the gross liability amount. Because the tax deductible prescription drug costs liability will be reduced by the subsidy, the deferred tax asset will be computed net of the subsidy, resulting in a lower deferred tax asset. The federal subsidy will not reduce the tax deductions until 2013. Even though the changes may not be effective until future periods, the effects are accounted for in the period that includes the enactment date. FASB ASC 715-60 discusses accounting and reporting guidance for other postretirement plans, including the Medicare prescription drug plan. Many public entities have already posted large noncash charges in early 2010 related to the nondeductibility of the subsidy.

.29 Some of the other provisions of the reform that may affect an entity's tax position include the nondeductible pharmaceuticals fee, the medical device excise tax, and the therapeutic discovery project tax credit, which will have an effect on the pharmaceutical and medical device industries. Additionally, employer group health plans may not impose lifetime limits and can only impose "restricted" annual limits beginning with the 2011 plan year (for calendar year plans); no annual limits would be permitted beginning in 2014. Because these health benefits can no longer be limited, entities may need to increase accruals for future medical obligations. Many small businesses and tax-exempt organizations that provide health insurance coverage to their employees will now qualify for a special tax credit that is designed to encourage small employers to offer health care coverage for the first time or maintain the coverage they have. Lastly, under the new reform, a 40 percent penalty will apply to tax understatements attributable to transactions lacking economic substance (20 percent with adequate disclosure) or failing to meet the requirements of any similar rule of law. A transaction is treated as having economic substance only if the transaction changes in a meaningful way (apart from federal income tax effects) the taxpayer's economic position, and the taxpayer has a substantial purpose (apart from federal income tax effects) for entering into the transaction.

.30 Additional items in the reform that may have favorable consequences for hospitals would include extending coverage for dependent children up to 26 years old, preventing health insurers from excluding children with preexisting conditions, providing access to health coverage through an interim high-risk pool for uninsured adults with preexisting conditions (which will be eliminated in 2014 when the state exchanges will become operational), and prohibiting the termination of existing coverage. Also, beginning in 2014, health insurers will be prohibited from excluding coverage for adults based on preexisting conditions, will have limits imposed on premium ratings, and must guarantee the issuance of coverage for anyone who seeks it.

.31 Other provisions include the following:

- Five-year demonstration grants provided to states to develop, implement, and evaluate alternatives to current tort litigations
- Ten percent Medicare bonus payments for primary care physicians
- Increased Medicaid payments to primary care physicians
- Increased federal oversight to screen procedures provided by providers to reduce fraud
- Reduced annual market basket updates for inpatient hospital, home health, skilled nursing facility, hospice, and other Medicare providers, adjusted for productivity
- Reduced reimbursement for Medicare advantage plans
- Medical loss ratio reports and rebates provided by health plan providers
- Grants provided to states to review and approve premium increases, which require plans to justify increases

.32 Entities will need to fully review the financial impact of the new law and consider disclosing possible future effects.

.33 The full text of these acts can be found at http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_public_laws&docid=f:publ152.111.pdf and http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_public_laws&docid=f:publ148.111.pdf.

The Dodd-Frank Wall Street Reform and Consumer Protection Act

.34 On July 21, 2010, the president signed the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) into law. The Dodd-Frank Act was approved by the House on June 30, before narrowly clearing the Senate on July 15. The Dodd-Frank Act will create new regulations for companies that extend credit to customers, exempt small public companies from Section 404(b) of the Sarbanes-Oxley Act of 2002 (SOX), make auditors of broker-dealers subject to Public Company Accounting Oversight Board (PCAOB) oversight, and change the registration requirements for investment advisers.

.35 Other requirements and additional information can be found in the full text of this act, which can be found at www.gpo.gov/fdsys/pkg/BILLS-111hr4173ENR/pdf/BILLS-111hr4173ENR.pdf. The AICPA is also following any developments related to the Dodd-Frank Act on our website at www.aicpa.org under "Advocacy—Federal Issues."

PCAOB Constitutionality

.36 On June 28, 2010, the Supreme Court ruled in the lawsuit challenging the constitutionality of the PCAOB. When the PCAOB was set up under SOX, its board members were appointed by the SEC and could be removed only for cause. The Supreme Court ruled in a 5-4 vote that although the manner in which the PCAOB was constituted was constitutionally invalid, SOX itself was not invalidated. Rather, the Supreme Court severed from the rest of SOX the provisions relating to the removal of PCAOB board members. The consequence of the Supreme Court's decision is that PCAOB board members will now be removable by the SEC at will, instead of only for good cause. Essentially, this decision has no material impact on the workings of the PCAOB, and all PCAOB programs will continue to operate as usual, including registration, enforcement, and standard-setting activities.

Municipal Securities Rulemaking Board Activity

.37 The Municipal Securities Rulemaking Board (MSRB) is a self-regulatory organization created by Congress in 1975 to protect investors and the public interest by developing rules for brokers, dealers, and municipal securities dealers (dealers) engaged in municipal securities activities. Under Rule 15c2-12(b)(5) of the Securities Exchange Act of 1934, an underwriter for a primary offering of municipal securities subject to the rule is prohibited from underwriting the offering unless the underwriter has determined that the issuer or an obligated person for whom financial information or operating data is presented in the final official statement has undertaken in writing to provide certain items of information to the MSRB. Rule 15c2-12(b)(5) provides that such items include (*a*) annual financial information concerning obligated persons; (*b*) audited financial statements for obligated persons if available and if not included in the annual financial information; (*c*) notices of certain events, if material; and (*d*) notices of failures to provide annual financial information on or before the date specified in the written undertaking.

.38 In 2009, the MSRB was designated by the SEC as the sole repository of these primary market and continuing disclosure documents. The MSRB's electronic repository and public website for these documents is known as the Electronic Municipal Market Access (EMMA) system.

Pending Proposal Regarding Continuing Disclosures

.39 In December 2009, the MSRB filed with the SEC an amendment to its pending July 2009 filing relating to additional voluntary submissions by issuers and obligated persons to the MSRB's EMMA system.

.40 The proposals would permit issuers to submit preliminary official statements and other primary market documents to EMMA. They would also permit issuers and obligated persons to voluntarily submit information relating to the preparation and submission of audited financial statements and annual financial information and to post links to other disclosure information (see MSRB Notice 2009-63). The MSRB has requested an effective date for the revised proposal to be announced by the MSRB in a notice published on the MSRB website at www.emma.msrb.org. This effective date shall be no later than 9 months after SEC approval of the revised proposal and shall be announced no later than 60 days prior to the effective date.

.41 The proposed December amendment, which revised the July proposal based on comments received by the SEC, would make the following key revisions to the original proposal.

Voluntary Annual Filing Undertaking

.42 The overall purpose of this undertaking is to assist investors and other market participants in understanding when the annual financial information required to be filed by issuers or obligated persons is expected to be available in the future. The original proposal would have consisted of a voluntary undertaking, either at the time of a primary offering or at any time thereafter, that the issuer or obligated person, as appropriate, would submit to EMMA of its annual financial information by no later than 120 calendar days after the end of the fiscal year. In light of the comments received on the July proposal, the MSRB modified the proposal to provide for a transitional option for issuers and obligated persons that would provide them the ability to indicate their undertaking to submit to EMMA the annual financial information by no later than 150 calendar days after the end of their fiscal year. However, on and after January 1, 2014, the transitional 150 day undertaking option would no longer be available for selection. An issuer or obligated person that wishes to could make the 120-day undertaking immediately upon the effectiveness of the revised proposal. The MSRB has stated that it contemplates that the making of a voluntary annual filing undertaking through EMMA by an issuer or obligated person would reflect the bona fide intent of the issuer or obligated person to perform as undertaken but would not, by itself, necessarily create a contractual obligation of such issuer or obligated person.

Voluntary Generally Accepted Accounting Principles Undertaking

.43 The overall purpose of this undertaking is to assist investors and other market participants in understanding how audited financial statements were prepared. The fact that an issuer or obligated person has entered into a voluntary generally accepted accounting principles (GAAP) undertaking and the standard under which audited financial statements are to be prepared would be prominently disclosed on the EMMA Web portal as a distinctive characteristic of the securities to which such undertaking applies. The voluntary GAAP undertaking would consist of a voluntary undertaking by an issuer or obligated person, either at the time of a primary offering or at any time thereafter, that the issuer or obligated person will prepare its audited financial statements in accordance with GAAP. In light of the comments received on the original proposal, the MSRB clarified that state or local governments or any other entities to which Governmental Accounting Standards Board (GASB) standards are applicable would apply GAAP as established by GASB and that any other entities to which FASB standards are applicable would apply GAAP as established by FASB.

Centers for Medicare and Medicaid Services Activity

Medicare and Medicaid Electronic Health Record Incentive Programs

.44 The nation's health care system is undergoing a transformation in an effort to improve quality, safety, and efficiency of care. To help facilitate this vision, the Health Information Technology for Economic and Clinical Health Act (HITECH Act) established programs under Medicare and Medicaid to provide incentive payments for the meaningful use of certified electronic health record (EHR) technology.

.45 The HITECH Act is expected to provide $20 billion to be invested in health IT infrastructure to encourage doctors and hospitals to use health IT to electronically exchange patients' health information, while saving $10 billion and generating additional savings throughout the health sector through improvements in quality of care and coordination and through reductions in medical errors and duplicative care.

.46 The Medicare and Medicaid EHR incentive programs will provide incentive payments to eligible professionals and eligible hospitals as they adopt, implement, upgrade, or demonstrate meaningful use of certified EHR technology. The incentive payments begin in 2011. For further information, visit www.cms.gov/EHRIncentivePrograms/.

ePrescribing Incentive Program

.47 The Centers for Medicare & Medicaid Services (CMS) offers eligible providers incentive payments when they use an electronic prescribing (e-prescribing) system to prescribe for Medicare patients. The CMS Electronic Prescribing Incentive Program was authorized by the Medicare Improvements for Patients and Providers Act of 2008, which became law on July 15, 2008. For 2009 and 2010, e-prescribing incentive amounts will be 2 percent of a provider's total estimated allowed charges for covered professional services during the reporting period. The incentive amount reduces to 1 percent in 2011 and finally to 0.5 percent in 2013.

.48 Changes to the program for 2010 include the following:

- Skilled nursing facility and home care are now eligible services.
- Eligible professionals need only report 25 separate electronic prescribing events during the reporting period.
- Eligible professionals will only report one G-code (G8553) that reflects at least one prescription created during the encounter was generated and transmitted electronically using a qualified electronic prescribing system.
- Data may be reported on the 2010 e-prescribing measure through claims, a qualified registry, or a qualified EHR product.

.49 Group practice changes for 2010 include the following:

- Group practices (200 or more eligible professionals) must be selected to participate in the Physician Quality Reporting Initiative (PQRI) group practice reporting option.
- Group practices must report the 2010 e-prescribing measure at least two and one-half times during the reporting period to be considered successful e-prescribers.
- Group practices may choose to report the e-prescribing measure through claims, a qualified registry, or a qualified EHR product.
- Group practices interested in participating in the 2010 PQRI through the group practice reporting option are required to submit a self-nomination letter to the CMS.

.50 For further information visit www.cms.gov.

IRS Activity

The Department of the Treasury and the IRS Issue a Priority Guidance Plan for 2010

.51 Fiscal year 2010 priorities are addressed through a flexible and interdisciplinary array of new tools that focus on enforcement of the tax law and improving customer service. Priorities include the following:

- Issuing guidance on program-related investments of private foundations

- Developing regulations on new excise taxes for donor-advised funds
- Issuing guidance for deferred compensation plans for NFPs
- A further focus on transparency and governance by tax-exempt entities
- Continued implementation of the online compliance guide, known as a *cyber assistant* (which is used to generate IRS Form 1023, "Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code," at a reduced user fee)
- Developing regulations regarding the extent to which a limited partner will be considered at risk with respect to liabilities of a partnership, including situations in which a limited partner may be obligated to contribute additional capital to the partnership in the future
- Issuing tax guidance regarding third-party payer issues and reporting agents

.52 Additional information on these and other topics is available at www.irs.gov/pub/irs-utl/2009_–_2010_priority_guidance_plan_initial.pdf.

New Health Insurance Tax Credit for Exempt Organizations

.53 Effective for tax year 2010, many small businesses and tax-exempt organizations that provide health insurance coverage to their employees now qualify for a special tax credit. Included in the health care reform legislation, the PPACA is a credit designed to encourage small employers to offer health care coverage for the first time or maintain their current coverage.

.54 To be eligible for the credit, a qualifying employer must cover at least 50 percent of the cost of health care coverage for some of its workers, based on the rate for single person coverage. A qualifying employer also must have less than the equivalent of 25 full-time workers (for example, an employer with fewer than 50 half-time workers may be eligible) and must pay average annual wages below $50,000 per full-time equivalent position.

.55 The credit is worth up to 35 percent of a small business's premium costs (25 percent for NFPs) in 2010. On January 1, 2014, this rate increases to 50 percent (35 percent for NFPs) but is subject to a phaseout. The credit phases out for entities with average wages between $25,000 and $50,000 and for entities with the equivalent of between 10 and 25 full-time workers.

.56 In September 2010, the IRS released a draft version of Form 8941, "Credit for Small Employer Health Insurance Premiums," which small businesses and tax-exempt organizations will use to calculate the small business health care tax credit when they file income tax returns next year. Small businesses will include the amount of the credit as part of the general business credit on their return, and tax-exempt organizations will claim the credit on a revised Form 990-T, "Exempt Organization Business Income Tax Return (and proxy tax under Section 6033(e))." For further information, visit www.irs.gov.

New Employment Tax Credits for Exempt Organizations

.57 Two new tax benefits are now available to nongovernmental employers hiring workers who were previously unemployed or only working part time.

These provisions are part of the Hiring Incentives to Restore Employment Act that was enacted into law in March 2010.

.58 Employers who hire unemployed workers after February 3, 2010, and before January 1, 2011, may qualify for a 6.2 percent payroll tax incentive, in effect exempting them from their share of Social Security taxes on wages paid to these workers after March 18, 2010. This reduced tax withholding will have no effect on the employee's future Social Security benefits, and employers would still need to withhold the employee's 6.2 percent share of Social Security taxes, as well as income taxes. The employer's and employee's share of Medicare taxes also would still apply to these wages.

.59 In addition, for each worker retained for at least 1 year, employers may claim an additional general business tax credit up to $1,000 per worker when they file their 2011 income tax returns.

.60 New hires filling existing positions also qualify but only if the workers they are replacing left voluntarily or for cause. Family members and other relatives do not qualify.

.61 In addition, the new law requires that the employer get a statement from each eligible new hire certifying that he or she was unemployed during the 60 days before beginning work or, alternatively, worked less than a total of 40 hours for someone else during the 60-day period. The IRS currently is developing a form that employees can use to make the required statement.

.62 Employers claim the payroll tax benefit on the federal employment tax return they file, usually quarterly, with the IRS. Eligible employers will be able to claim the new tax incentive on their revised employment tax form for the second quarter of 2010. Revised forms and further details on these two new tax provisions will be posted on www.irs.gov.

Internet-Based Workshop for Exempt Entities

.63 The IRS has an Internet-based version of its popular "Exempt Organizations Workshop" covering tax compliance issues confronted by small and midsized tax-exempt entities.

.64 The free online workshop, "Stay Exempt—Tax Basics for Exempt Organizations," consists of the following five interactive modules on tax compliance topics for exempt entities:

- *Tax-Exempt Status.* How can you keep your 501(c)(3) exempt?
- *Unrelated Business Income.* Does your entity generate taxable income?
- *Employment Issues.* How should you treat your workers for tax purposes?
- *Form 990.* Would you like to file an error-free return?
- *Required Disclosures.* To whom do you have to show your records?

.65 Users can access this new training program at www.stayexempt.org. Users can complete the modules in any order and repeat them as many times as they like. The online training website does not require registration, and its visitors will remain anonymous. The workshop can be found at www.stayexempt.org/Virtual-Workshop.aspx.

Resource Materials—Compliance Initiatives for Tax-Exempt Entities

.66 The Exempt Organizations Division of the IRS has made materials available that were used in, or which discuss, its compliance initiatives, including limited liability company projects, community foundations, bond compliance, hospitals, and executive compensation. You can find this material at www.irs.gov/charities/article/0,,id=162493,00.html.

Listing of Published Guidance—2010

.67 Readers should be aware that the IRS website contains a digest of published guidance for tax-exempt entities issued in 2010 at www.irs.gov/charities/content/0,,id=202419,00.html. The published guidance includes treasury regulations, revenue rulings, revenue procedures and notices, and announcements of recently published issues of interest to tax-exempt entities.

.68 The IRS website also contains an archive that presents digests of IRS-published guidance of interest to tax-exempt entities for the years 1954–2009. The archived guidance can be found at www.irs.gov/charities/article/0,,id=151053,00.html. Additionally, the IRS has a useful tool for NFPs to assist them in maintaining their tax-exempt status through compliance with IRS requirements. The publication *Compliance Guide for 501(c)(3) Public Charities* is available at www.irs.gov/pub/irs-pdf/p4221pc.pdf.

IRS Notice 2010-39, Request for Comments Regarding Additional Requirements for Tax-Exempt Hospitals

.69 IRS Notice 2010-39, *Request for Comments Regarding Additional Requirements for Tax-Exempt Hospitals*, solicits comments regarding the application of certain requirements imposed by new Section 501(r) added to the IRC by section 9007(a) of the PPACA. This section affects hospital organizations that are currently described in Section 501(c)(3) of the IRC as exempt from federal income taxation.

.70 New Section 501(r)(1) imposes four additional requirements that hospital organizations must satisfy to be described as tax exempt: (*a*) conducting a community health needs assessment every three years and adopting an implementation strategy to meet the needs identified through the assessment, (*b*) establishing a financial assistance policy and a policy relating to emergency care, (*c*) certain limitations on amounts charged for emergency or other medically necessary care to individuals eligible for assistance, and (*d*) certain restrictive requirements for collection processes on individuals who may be eligible for financial assistance.

.71 The PPACA also added new Section 4959, which imposes an excise tax for failures to meet certain of the new Section 501(r) requirements, and reporting requirements under Section 6033(b) related to Sections 501(r) and 4959.

.72 Readers should be aware of the final ruling available at www.irs.gov.

New Filing and Audit Requirements for Employee Retirement Income Security Act-Covered Section 403(b) Employee Benefit Plans

.73 Beginning in 2009, employee benefit plans sponsored by charitable entities and schools under IRC Section 403(b) and covered under the

Employee Retirement Income Security Act of 1974 (ERISA) were subject to the same reporting and audit requirements as Section 401(k) plans. Section 403(b) plans also are commonly known as *tax-shelter annuity plans*. Under Department of Labor (DOL) regulations issued in November 2007 amending the filing requirements for Form 5500, "Annual Return/Report of Employee Benefit Plan," ERISA-covered Section 403(b) plans with 100 or more participants generally are required to file audited financial statements beginning with their 2009 Form 5500 filing. Section 403(b) plans with fewer than 100 participants are eligible to use abbreviated reporting forms without audited financial statements. The DOL estimates that approximately 7,000 Section 403(b) plans are subject to the new audit requirements, and another 9,000 Section 403(b) plans will be eligible for the waiver. The DOL regulations were published in the November 16, 2007, *Federal Register* and are available at www.dol.gov/ebsa/regs/fedreg/final/20071116.pdf. The AICPA Employee Benefit Plan Audit Quality Center (www.aicpa.org/EBPAQC) and Expert Panel have formed a joint task force to develop resources to help members with these audit requirements.

Red Flags Rule

.74 In October 2007, the Federal Trade Commission (FTC) issued the Red Flags Rule for financial institutions and creditors to fight identity theft. The rule sets out how certain businesses and organizations must develop, implement, and administer their identity theft prevention programs. These programs must include the following four basic elements, which, together, create a framework to address the threat of identity theft:

- The program must include reasonable policies and procedures to identify the red flags of identity theft that may arise in the day-to-day operation of your business. *Red flags* are suspicious patterns or practices or specific activities that indicate the possibility of identity theft. For example, if a customer has to provide some form of identification to open an account with an entity, an ID that looks like it might be fictitious would be a red flag.
- The program must be designed to detect the red flags that have been identified. For example, if an entity has identified fake IDs as a red flag, it must have procedures in place to detect possible fake, forged, or altered identification.
- The program must spell out appropriate actions to take when red flags are detected.
- The program must address how the program will be reevaluated periodically to reflect new risks from this crime because identity theft is an ever-changing threat.

.75 The program must state who is responsible for implementing and administering it effectively. Because employees have a role to play in preventing and detecting identity theft, the program also must include appropriate staff training. The program also must address the manner in which contractors will be monitored when outsourcing or subcontracting functions of operations that would be covered by the rule.

.76 The Red Flags Rule applies to financial institutions and creditors. The rule requires a periodic risk assessment to determine if the entity has covered accounts. A written program needs to be in place only if the entity has covered accounts. It is important to look closely at how the rule defines *financial institution* and *creditor* because the terms apply to groups that typically might not use those words to describe themselves. For example, many NFPs and government agencies are creditors under the rule.

.77 The Red Flags Rule does not name specific types of organizations that must comply; however, for NFP organizations, compliance requirements are based on the types of accounts that the institution has with its customers and clients. Examples include (*a*) payment plans for tuition at a college or university or (*b*) club dues of an NFP that are allowed to be paid in installments. Because of their creditor status in these situations, the Red Flags Rule applies.

.78 The FTC suspended enforcement of the new Red Flags Rule until June 10, 2010. After June 10, 2010, any instance of identity theft exposes the NFP organization to an FTC investigation.

.79 More information and a document outlining specific requirements of the Red Flags Rule can be found at http://ftc.gov/redflagsrule.

Audit and Attestation Issues and Developments

Audit Risks Arising From Current Economic Conditions

.80 The recent economic conditions and regulatory actions described in this alert may cause additional risk factors that had not previously existed or did not have a material effect on audit clients in prior years. Some risks that may affect an entity in the current economic environment are as follows:

- Marginally achieving explicitly stated strategic objectives
- Volatile real estate and business markets
- Significant measurement uncertainty, including accounting estimates and fair value measurements
- Potentially erroneous or fraudulent activity due to decreased staffing and resurgence of business activity
- The continuing evolution of the postrecessionary marketplace

.81 Although many of these risks are not new to businesses, consideration of the ways a client is affected by external forces is part of obtaining an understanding of the entity and its environment and will allow the auditor to plan and perform the audit to address those risks. As noted in paragraph .17 of AU section 312, some possible audit responses to significant risks of material misstatement include increasing the extent of audit procedures, performing procedures closer to year-end, or increasing audit procedures to obtain more persuasive evidence. Additionally, given the constant changing status of economic conditions that could affect your client, auditors should consider modifying audit procedures to ensure that risks are still adequately addressed.

.82 Although it is impossible to predict and include all accounting, auditing, and attestation issues that may affect your engagements, we cover in this alert the primary areas of concern. Continue to remain alert to economic, legislative, and regulatory developments, as well as the associated accounting, auditing, and attestation issues as you perform your engagements.

PCAOB Auditing Standards on Risk Assessment

.83 In August 2010, the PCAOB adopted a suite of eight auditing standards related to the auditor's assessment of, and response to, risk in an audit. These standards were initially proposed in late 2008 and reproposed in late 2009. These risk assessment standards will benefit investors by setting forth requirements that enhance the effectiveness of the auditor's assessment of, and response to, the risks of material misstatement in the financial statements. They are applicable to audit procedures spanning from the initial planning stages of the audit to the evaluation of the audit results. Improvements in the risk assessment standards should enhance integration of the audit of financial statements with the audit of internal control over financial reporting by articulating a process for identifying and assessing risks of material misstatements that apply to both portions of the integrated audit.

.84 The new auditing standards, with a brief description of each, are as follows:

- Auditing Standard No. 8, *Audit Risk*, discusses the auditor's consideration of audit risk in both an integrated audit and an audit of financial statements only. It describes the components of audit risk and the auditor's responsibilities for reducing it to an appropriately low level.
- Auditing Standard No. 9, *Audit Planning*, establishes requirements for planning an audit, such as assessing important matters and establishing an appropriate audit strategy.
- Auditing Standard No. 10, *Supervision of the Audit Engagement*, is applicable to the engagement partner and other team members who supervise during the audit. It sets forth requirements for supervision of the audit engagement and the work of other engagement members. Related to this topic, the PCAOB also recently issued a release discussing the provision of SOX that authorizes the PCAOB to impose sanctions on registered public accounting firms and their supervisory personnel for failing to reasonably supervise associated persons.
- Auditing Standard No. 11, *Consideration of Materiality in Planning and Performing an Audit*, describes the auditor's responsibilities for consideration of materiality in planning and performing an audit.
- Auditing Standard No. 12, *Identifying and Assessing Risks of Material Misstatement*, establishes requirements for auditors in identifying and assessing risks of material misstatement, including information-gathering procedures.
- Auditing Standard No. 13, *The Auditor's Responses to the Risks of Material Misstatement*, establishes requirements for responding to those identified risks of material misstatement through general audit procedures. It also includes audit procedures related to significant accounts and disclosures.
- Auditing Standard No. 14, *Evaluating Audit Results*, establishes requirements for evaluating audit results and the sufficiency of appropriate audit evidence.

- Auditing Standard No. 15, *Audit Evidence*, discusses what constitutes audit evidence and how to design and perform audit procedures to support the opinion expressed in the auditor's report.

.85 These risk assessment standards will supersede the following six PCAOB interim standards and related amendments: AU-P section 311, *Planning and Supervision*; AU-P section 312, *Audit Risk and Materiality in Conducting an Audit*; AU-P section 313, *Substantive Tests Prior to the Balance Sheet Date*; AU-P section 319, *Consideration of Internal Control in a Financial Statement Audit*; AU-P section 326, *Evidential Matter*; and AU-P section 431, *Adequacy of Disclosure in Financial Statements* (AICPA, *PCAOB Standards and Related Rules*, Standards). The standards, if approved by the SEC, will be effective for audits of fiscal periods beginning on or after December 15, 2010.

Engagement Quality Review for Issuers

.86 In January 2010, the PCAOB announced that the SEC had approved Auditing Standard No. 7, *Engagement Quality Review* (AICPA, *PCAOB Standards and Related Rules*, Standards, AU-P sec. 162), which was adopted by the PCAOB in July 2009. Auditing Standard No. 7 (AU-P sec. 162) provides a framework for the engagement quality reviewer to objectively evaluate the significant judgments made and related conclusions reached by the engagement team in forming an overall conclusion about the engagement. Auditing Standard No. 7 (AU-P sec. 162) is expected to increase the likelihood that a registered public accounting firm will catch any significant deficiencies before it issues its audit report. As a result, more work may be necessary under this standard than performed under the existing requirements for concurring partners. However, Auditing Standard No. 7 (AU-P sec. 162) explains that the procedures required by the engagement quality reviewer are different in nature than those required to be performed by the engagement team. Further, if the engagement quality reviewer deems more work is required before giving approval of issuance, the engagement team is responsible for completing that work.

.87 This standard applies to all audit engagements, and engagements to review interim financial information, conducted pursuant to the standards of the PCAOB, and it supersedes the PCAOB's interim concurring partner review requirement. Auditing Standard No. 7 (AU-P sec. 162) is effective for engagement quality reviews of audits and interim reviews for fiscal years that began on or after December 15, 2009. For a public, calendar-year company, this standard is applicable for the quarter ended March 31, 2010. Subsequent to the issuance of Auditing Standard No. 7 (AU-P sec. 162), the PCAOB issued Staff Question and Answer, *Auditing Standard No. 7,* Engagement Quality Review (AICPA, *PCAOB Standards and Related Rules*, PCAOB Staff Guidance, sec. 100.10), to provide further implementation guidance on the documentation requirements of the standard. For the full text of the standard and the question and answer, readers are encouraged to visit the PCAOB's website at www.pcaob.org.

Supplementary and Other Information Related to Financial Statements

.88 In February 2010, the AICPA Auditing Standards Board (ASB) issued a trio of auditing standards related to the auditor's responsibility for other information, supplementary information, and required supplementary information. These three standards supersede AU section 550A, *Other Information in Documents Containing Audited Financial Statements*; AU section

551A, *Reporting on Information Accompanying the Basic Financial Statements in Auditor-Submitted Documents*; and AU section 558A, *Required Supplementary Information* (AICPA, *Professional Standards*, vol. 1). All three standards are effective for audits of financial statements for periods beginning on or after December 15, 2010. Early application is permitted.

Other Information in Documents Containing Audited Financial Statements

.89 Statement on Auditing Standards (SAS) No. 118, *Other Information in Documents Containing Audited Financial Statements* (AICPA, *Professional Standards*, vol. 1, AU sec. 550), addresses the auditor's responsibility in relation to other information in documents containing audited financial statements and the auditor's report thereon. In this SAS, *other information* is defined as financial and nonfinancial information (other than the financial statements and the auditor's report thereon) that is included in a document containing audited financial statements and the auditor's report thereon, excluding required supplementary information. *Documents containing audited financial statements* refers to annual reports (or similar documents) that are issued to owners (or similar stakeholders) and annual reports of governments and organizations for charitable or philanthropic purposes that are available to the public that contain audited financial statements and the auditor's report thereon. In the absence of any separate requirement in the particular circumstances of the engagement, the auditor's opinion on the financial statements does not cover other information, and the auditor has no responsibility for determining whether such information is properly stated. This SAS establishes the requirement for the auditor to read the other information of which the auditor is aware because the credibility of the audited financial statements may be undermined by material inconsistencies between the audited financial statements and other information. This SAS also may be applied, adapted as necessary in the circumstances, to other documents to which the auditor, at management's request, devotes attention.

Supplementary Information in Relation to the Financial Statements as a Whole

.90 SAS No. 119, *Supplementary Information in Relation to the Financial Statements as a Whole* (AICPA, *Professional Standards*, vol. 1, AU sec. 551), addresses the auditor's responsibility when engaged to report on whether supplementary information is fairly stated, in all material respects, in relation to the financial statements as a whole. For purposes of generally accepted auditing standards (GAAS), *supplementary information* is defined as information presented outside the basic financial statements, excluding required supplementary information that is not considered necessary for the financial statements to be fairly presented in accordance with the applicable financial reporting framework. Such information may be presented in a document containing the audited financial statements or separate from the financial statements.

.91 The information covered by this SAS is presented outside the basic financial statements and is not considered necessary for the financial statements to be fairly presented in accordance with the applicable financial reporting framework. This SAS also may be applied, with the report wording adapted as necessary, when an auditor has been engaged to report on whether required supplementary information is fairly stated, in all material respects, in relation to the financial statements as a whole.

Required Supplementary Information

.92 SAS No. 120, *Required Supplementary Information* (AICPA, *Professional Standards*, vol. 1, AU sec. 558), addresses the auditor's responsibility with respect to *required supplementary information*. The SAS defines *required supplementary information* as information that a designated accounting standard setter requires to accompany an entity's basic financial statements. Required supplementary information is not part of the basic financial statements; however, a designated accounting standard setter considers the information to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. In addition, authoritative guidelines for the methods of measurement and presentation of the information have been established. In the absence of any separate requirement in the particular circumstances of the engagement, the auditor's opinion on the basic financial statements does not cover required supplementary information. SAS No. 120 explains that the objectives of the auditor, when a designated accounting standard setter requires information to accompany an entity's basic financial statements, are to perform specified procedures in order to

- describe, in the auditor's report, whether required supplementary information is presented and
- communicate therein when some or all of the required supplementary information has not been presented in accordance with guidelines established by a designated accounting standard setter or when the auditor has identified material modifications that should be made to the required supplementary information for it to be in accordance with guidelines established by the designated accounting standard setter.

Auditing Fair Value Measurements

.93 In addition to understanding the looming questions relative to fair value accounting, auditors should be aware of audit issues involving fair value measurements. Particular assets, liabilities, and components of equity are measured or disclosed at fair value in the financial statements, and it is management's responsibility to make the fair value measurements and disclosures. When auditing these fair values to ensure they are in conformity with U.S. GAAP, auditors should consult AU section 328, *Auditing Fair Value Measurements and Disclosures* (AICPA, *Professional Standards*, vol. 1), which establishes standards and provides guidance for auditors. Specific types of fair value measurements are not covered by AU section 328. For example, when auditing the fair value of derivatives and securities, refer to AU section 332, *Auditing Derivative Instruments, Hedging Activities, and Investments in Securities* (AICPA, *Professional Standards*, vol. 1).

.94 In regard to analyzing the sufficiency of the audit evidence, the strongest audit evidence to support a fair value is an observable market price in an active market. If that is not available, a valuation method should incorporate common market assumptions. If common market assumptions are not available or require significant adjustments, the entity may use its own assumptions. The auditor should obtain an understanding of the entity's process for determining fair values, as well as whether the fair value measurements and disclosures are in accordance with U.S. GAAP. During this testing, the auditor also may identify any possible indicators of impairment. According to paragraph .23 of

AU section 328, substantive tests of the fair value measurements may involve (*a*) testing management's significant assumptions, the valuation model, and the underlying data; (*b*) developing independent fair value estimates for corroborative purposes; or (*c*) reviewing subsequent events and transactions. Paragraph .26 also notes that when testing the fair value measurements and disclosures, the auditor should evaluate whether management's assumptions are reasonable and reflect, or are not inconsistent with, market information. According to FASB ASC 820, *Fair Value Measurements and Disclosures*, under U.S. GAAP this may include evaluating the following:

- Whether a significant decrease has occurred in the volume and level of activity for the asset or liability when compared with normal market activity, which may include consideration of the number of recent transactions, the date of the most recent price quotes, consistency among price quotes, increases in implied liquidity risk premiums, increases in the bid-ask spread, and the amount of publicly available information.
- Whether the transaction was an orderly transaction, which may include consideration of the seller's financial condition, the counterparty credit position, the exposure to the market during the marketing period, and the actual transaction price.
- The reasonableness of the underlying assumptions, which may include consideration of the use of pricing services, the assumptions used by the pricing service, and the extent of testing required to verify the reasonableness of the prices provided. (For example, the auditor should understand whether the fair value measurement was determined using quoted prices from an active market, observable inputs, or fair value measurements based on a model. If the price is not based on quoted prices from an active market or observable inputs, the auditor should obtain an understanding of the model used by the pricing service and evaluate whether the assumptions are reasonable [see the following section for additional information on pricing services].)
- The reasonableness of the determination within the fair value hierarchy of inputs.

Fair Values of Securities

.95 The guidance in AU section 332 relating to auditing the fair value of securities is fairly similar to the guidance in AU section 328; however, there are some items of note for the auditor. As previously mentioned, quoted market prices in active markets are the best available audit evidence to support a fair value; however, when they are unavailable and the valuations of securities are obtained from a broker or dealer or another pricing service based on valuation models, the auditor should understand the underlying valuation method used (such as a cash flow projection). These prices also may be based on quoted prices from an active market or other observable inputs that will be a consideration on the auditor's procedures. The process used by the pricing service in measuring fair value should be evaluated to determine the consistency with the specified valuation method (as discussed in FASB ASC 820-10-35). The auditor also may determine that it is necessary to obtain quotes from more than one pricing source based on circumstances, such as an existing relationship between the entity and the valuing entity, which could inhibit objective pricing or underlying valuation assumptions that are highly subjective. In the context of FASB ASC 820, quoted prices in active markets are considered level 1 inputs.

.96 When an entity performs its own valuation, value testing procedures include the following:

- Assessing the reasonableness
- Comparing the assumptions to industry reports or benchmarks
- Assessing the appropriateness of the model
- Calculating the value using his or her own model
- Comparing the fair value with subsequent or recent transactions

.97 Whether the inputs to the entity's valuation model are observable determines their characterization as level 2 or level 3 inputs, respectively, within FASB ASC 820. When extensive judgment is needed, consider using a specialist or refer to AU section 342, *Auditing Accounting Estimates* (AICPA, *Professional Standards*, vol. 1). Additionally, when the underlying collateral of a security significantly contributes to its fair value and collectability of the security, evidence of the collateral also should be examined for existence, fair value, transferability, and the investor's right to the collateral.

.98 Paragraph .19 of AU section 328 also notes that the auditor should evaluate whether the entity's method for determining fair value measurements is applied consistently and, if so, whether the consistency is appropriate considering possible changes in the environment or circumstances affecting the entity or changes in accounting principles. The auditor also should evaluate management's conclusions regarding other-than-temporary impairment on its securities. Examples of factors that could cause an other-than-temporary impairment, per paragraph .47 of AU section 332, include the following:

- Fair value is significantly below cost and
  - — the decline is attributable to adverse conditions specifically related to the security or to specific conditions in an industry or in a geographic area.
  - — the decline has existed for an extended period of time.
  - — management does not possess both the intent and the ability to hold the security for a period of time sufficient to allow for any anticipated recovery in fair value.
- The security has been downgraded by a rating agency.
- The financial condition of the issuer has deteriorated.
- Dividends have been reduced or eliminated, or scheduled interest payments have not been made.
- The entity recorded losses from the security subsequent to the end of the reporting period.

.99 Auditors should consider all facts and circumstances when determining if an other-than-temporary impairment has occurred. Additionally, the classification of an entity's securities is based on management's intent and ability. The auditor should obtain an understanding of management's classification process among trading, available-for-sale, and held-to maturity, as well as consider the classifications in light of the entity's current financial position.

Auditing Accounting Estimates

.100 As noted in paragraph .04 of AU section 342, the auditor is responsible for evaluating the reasonableness of accounting estimates made by management in the context of the financial statements as a whole. Although this alert has discussed fair value measurements at length, it is important to remember many types of accounting estimates exist in client financial statements. Some examples include the allowance for uncollectible accounts receivable, impairment analysis and estimated useful lives of long lived assets, valuation allowance for deferred tax assets, and actuarial assumptions in pension and other postretirement benefit costs.

.101 Given the current economic climate, additional skepticism should be exercised when considering management's underlying assumptions used in accounting estimates. When evaluating accounting estimates, the auditor should consider both the subjective and objective factors with professional skepticism. As discussed in paragraph .09 of AU section 342, key factors and assumptions that the auditor normally concentrates on include the assumptions that are significant to the estimate, sensitive to variations, deviations from historical patterns, or particularly subjective and susceptible to misstatement and bias; however, it is important to consider whether historical patterns are still applicable.

.102 For example, in the current market, new patterns may emerge. In this economic climate, with possible increasing pressure on management to meet earnings, a key aspect of AU section 342 is for an auditor to determine the reasonableness of management's accounting estimates with an extra degree of professional skepticism. As noted by AU section 316, *Consideration of Fraud in a Financial Statement Audit* (AICPA, *Professional Standards*, vol. 1), when assessing audit differences between client estimates and audit estimates, even if they are individually reasonable, an auditor should consider whether these differences are indicative of possible bias by management. If so, the auditor should reconsider the estimates as a whole.

.103 The auditor should obtain an understanding of how management develops estimates and should employ one of the approaches outlined in paragraph .10 of AU section 342 in testing that process. In reviewing and testing management's process, the auditor may consider identifying controls around this process and determining if the underlying data used for the estimate are reliable and used appropriately. An auditor also may develop an estimate and compare it to management's estimate. Lastly, the auditor may review subsequent events or transactions occurring prior to the date of the auditor's report. Further, as noted in AU section 316, hindsight may provide the auditor additional insight into the existence of management bias. For further details on auditing estimates, see AU section 342. The AICPA has released a proposed redrafted SAS, *Auditing Accounting Estimates, Including Fair Value Accounting Estimates and Related Disclosures* (Redrafted), on auditing accounting estimates, including fair value. Readers are encouraged to remain alert for developments on this topic.

Using the Work of a Specialist

.104 It may be necessary to use a specialist (such as a securities valuation expert) to assist in auditing complex or subjective matters. Examples of matters in which an auditor may engage a specialist are valuation issues;

reasonableness of determination of amounts derived from specialized techniques or models; or implementation of technical requirements, regulations, or legal documents. AU section 336, *Using the Work of a Specialist* (AICPA, *Professional Standards*, vol. 1), provides guidance to auditors in using specialists. The guidance in AU section 336 is applicable when the specialist is hired by management or if the auditor engages the specialist. However, if a specialist employed by the auditor's firm participates in the audit, AU section 311, *Planning and Supervision* (AICPA, *Professional Standards*, vol. 1), is applicable rather than AU section 336.

.105 When using the work of a specialist, the auditor should evaluate the specialist's professional qualifications, obtain an understanding of the nature of the work performed or to be performed, and evaluate the relationship of the specialist to the client in terms of objectivity. Although the appropriateness and reasonableness of the methods and assumptions employed by the specialist are his or her responsibility, the auditor should obtain an understanding of these qualities, test the underlying data provided to the specialist, and evaluate the specialist's findings in the context of the audit and related assertions in the financial statements. In July 2010, the PCAOB issued Staff Audit Practice Alert No. 6, *Auditor Considerations Regarding Using the Work of Other Auditors and Engaging Assistants from Outside the Firm* (AICPA, *PCAOB Standards and Related Rules*, PCAOB Staff Guidance, sec. 400.06), because it observed that a number of registered public accounting firms located in the United States have been issuing audit reports on financial statements filed by issuers that have substantially all of their operations outside of the United States. Auditors of issuers should consult this practice alert for reminders concerning their obligations when using the work of other firms or using assistants engaged from outside the firm, such as in the aforementioned situation.

Communicating Internal Control Related Matters Identified in an Audit

.106 SAS No. 115, *Communicating Internal Control Related Matters Identified in an Audit* (AICPA, *Professional Standards*, vol. 1, AU sec. 325), supersedes SAS No. 112, *Communicating Internal Control Related Matters Identified in an Audit*, and further clarifies standards and provides guidance on communicating matters related to an entity's internal control over financial reporting (internal control) identified in an audit of financial statements. SAS No. 115 is effective for audits of financial statements for periods ending on or after December 15, 2009, with early implementation permitted.

.107 The SAS is applicable whenever an auditor expresses an opinion on financial statements (including a disclaimer of opinion), except when the auditor is performing an integrated audit and will be expressing an opinion on the effectiveness of internal control over financial reporting under AT section 501, *An Examination of an Entity's Internal Control Over Financial Reporting That Is Integrated With an Audit of Its Financial Statements* (AICPA, *Professional Standards*, vol. 1). In general, SAS No. 115 retains many of the provisions of SAS No. 112. The key differences between the two standards lie in the definitions of *material weaknesses* and *significant deficiencies*.

Definitions of Significant Deficiency *and* Material Weakness

.108 A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that a reasonable possibility exists that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. For the purpose of this definition, a reasonable possibility exists when the likelihood of the event is either *reasonably possible* or *probable*, as those terms are defined in the FASB ASC glossary. The FASB ASC glossary defines *reasonably possible* as when the chance of the future event or events occurring is more than remote but less than likely; *probable* is defined as when the future event or events are likely to occur. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness yet important enough to merit attention by those charged with governance.

The Evaluation Process

.109 Although the auditor is not required to perform procedures specifically to identify deficiencies in internal control, during the course of the audit, the auditor may become aware of deficiencies in the design or operation of the entity's internal control. The auditor should evaluate the severity of each deficiency in internal control identified during the audit and determine whether the deficiency, individually or in combination with other deficiencies in internal control, rise to the level of significant deficiencies or material weaknesses. Further, the severity of a deficiency does not depend on whether a misstatement actually occurred.

.110 The AICPA published the Audit Risk Alert *Communicating Internal Control Related Matters in an Audit—Understanding SAS No. 115* (product no. 022539) to assist in understanding the requirements of this SAS. This Audit Risk Alert provides specific case studies to help determine whether identified control weaknesses would constitute a significant deficiency or material weakness; it can be obtained by calling the AICPA at (888) 777-7077 or visiting www.cpa2biz.com.

Service Organizations

.111 Since 1992, SAS No. 70, *Service Organizations* (AICPA, *Professional Standards*, vol. 1, AU sec. 324) has been the authoritative standard on requirements and guidance for reporting on controls at service organizations and auditing the financial statements of entities that use service organizations to accomplish tasks that may affect their financial statements. This guidance has now been split into an attest standard and an auditing standard to better reflect the nature of the work being performed. Statement on Standards for Attestation Engagements (SSAE) No. 16, *Reporting on Controls at a Service Organization* (AICPA, *Professional Standards*, vol. 1, AT sec. 801), contains the requirements for reporting on controls at service organizations that are relevant to user entities' internal control over financial reporting. A finalized clarified SAS on service organizations, *Audit Considerations Relating to an Entity Using a Service Organization*, will supersede SAS No. 70 and addresses the user auditor's responsibility for obtaining sufficient appropriate audit evidence in an audit of the financial statements of a user entity that uses one or more service organizations. This SAS will be effective for audits of financial statements for periods ending on or after December 15, 2012. SSAE No. 16 is effective for service auditor's reports for periods ending on or after June 15, 2011. Until the new SAS is effective, user auditors will still use the guidance currently contained in AU section 324. Once the new SAS becomes effective, it will replace the guidance for user auditors currently in AU section 324. SSAE No. 16 is based on the International Auditing and Assurance Standards Board's (IAASB's) International

Standard on Assurance Engagements No. 3402, *Assurance Reports on Controls at a Service Organization*, and the new SAS is based on the IAASB's International Standard on Auditing (ISA) 402, *Audit Considerations Relating to an Entity Using a Service Organization*.

.112 The AICPA is in the process of overhauling and rewriting the Audit Guide *Service Organizations: Applying SAS No. 70, as Amended* (commonly known as the SAS 70 guide). Also, to address reporting on a service provider's controls over subject matter other than financial reporting, the AICPA is developing a new Audit Guide, *Reporting on Controls at a Service Provider Relevant to Security, Availability, Processing Integrity, Confidentiality, or Privacy*. Both guides are expected to be available for sale in early 2011. The AICPA is also in the process of drafting communication materials that will help auditors, clients, and users understand the three types of service organization control (SOC) reports (formerly SAS No. 70 reports) to be used for reporting on these engagements.

	Title	***Description***
SOC 1	*Report on Controls at a Service Organization Relevant to User Entities' Internal Control over Financial Reporting*	To be used only in circumstances when the service organization's services and controls affect the internal control over financial reporting for the entities that use the service.
SOC 2	*Report on Controls at a Service Organization Relevant to Security, Availability, Processing Integrity, Confidentiality, and Privacy*	The purpose is to convey trust and assurance to users of the system that the service organization has deployed an effective control system to effectively mitigate operational and compliance risks that the system may represent to its users.
SOC 3	*Trust Services Report*	These reports are designed to meet the needs of users who want assurance on the controls at a service organization related to security, availability, processing integrity, confidentiality, or privacy of a system but do not have the need for the level of detail provided in an SOC 2 report. These reports are general use reports and can be freely distributed or posted on a website as a seal.

Compilation and Review Engagements

.113 The AICPA developed a brand new guide, *Compilation and Review Engagements*, which provides additional information on implementing Statement on Standards for Accounting and Review Services No. 19, *Compilation and Review Engagements* (AICPA, *Professional Standards*, vol. 2). It also includes illustrative engagement and representation letters, sample compilation and review reports, detailed illustrations, and case studies. This guide is now available electronically and in paperback on www.cpa2biz.com.

Accounting Issues and Developments

.114 Given the current economic climate, auditors should consider a number of accounting and financial reporting issues, such as the following:

- Fair value, including fair value measurements in illiquid markets
- Impairment

Presentation of Insurance Claims and Related Recoveries

.115 In August 2010, FASB issued ASU No. 2010-24, *Health Care Entities (Topic 954): Presentation of Insurance Claims and Related Insurance Recoveries (a consensus of the Emerging Issues Task Force)*, to address current diversity in practice related to the accounting by health care entities for medical malpractice claims and similar liabilities and their related anticipated insurance recoveries. Most health care entities have netted anticipated insurance recoveries against the related accrued liability, although some have presented the anticipated insurance recovery and related liability on a gross basis.

.116 The amendments in ASU No. 2010-24 are consistent with the guidance on netting receivables and payables in FASB ASC 210-20 that is more broadly applicable for entities in other industries and that does not permit offsetting of conditional or unconditional liabilities with anticipated insurance recoveries from third parties.

.117 ASU No. 2010-24 clarifies that a health care entity should not net insurance recoveries against a related claim liability, and the claim liability should be determined without consideration of insurance recoveries.

.118 The amendments in ASU No. 2010-24 are effective for fiscal years beginning after December 15, 2010, and interim periods within those fiscal years. A cumulative-effect adjustment should be recognized in opening retained earnings in the period of adoption if a difference exists between any liabilities and insurance receivables recorded as a result of application. Retrospective and early application are permitted.

Measuring Charity Care for Disclosure

.119 In August 2010, FASB issued ASU No. 2010-23, *Health Care Entities (Topic 954): Measuring Charity Care for Disclosure—a consensus of the FASB Emerging Issues Task Force*, to reduce the diversity in practice regarding the measurement basis used in the disclosure of charity care. Some entities determine their charity care disclosures on the basis of a cost measurement, and others use a revenue measurement.

.120 ASU No. 2010-23 requires that cost be used as the measurement basis for charity care disclosure purposes and that cost be identified as the direct and indirect costs of providing charity care. Because various techniques will likely be used to determine how the direct and indirect costs are identified, such as obtaining the information directly from a costing system or through reasonable estimation techniques, ASU No. 2010-23 also requires the disclosure of the method used to identify or determine costs.

.121 The amendments of ASU No. 2010-23 are effective for fiscal years beginning after December 15, 2010, and should be applied retrospectively. Early application is permitted.

FASB Statement No. 168

.122 FASB Statement No. 168, *The* FASB Accounting Standards Codification™ *and the Hierarchy of Generally Accepted Accounting Principles—a replacement of FASB Statement No. 162*, as codified in FASB ASC 105, *Generally Accepted Accounting Principles*, is effective for financial statements issued for interim and annual periods ending after September 15, 2009. On the effective date of FASB Statement No. 168, FASB ASC became the source of authoritative U.S. accounting and reporting standards for nongovernmental entities, in addition to guidance issued by the SEC. FASB ASC superseded all then-existing, non-SEC accounting and reporting standards for nongovernmental entities. This new standard flattens the U.S. GAAP hierarchy to two levels: one that is authoritative (in FASB ASC) and one that is nonauthoritative (not in FASB ASC). Exceptions include all rules and interpretive releases of the SEC under the authority of federal securities laws, which are sources of authoritative U.S. GAAP for SEC registrants, and certain grandfathered guidance having an effective date before March 15, 1992. If an accounting change results from the application of this guidance, an entity should disclose the nature and reason for the change in accounting principle in their financial statements.

Referencing FASB ASC in Your Documentation

.123 You should consider how your entity will reference FASB ASC in your documentation (policy and procedures, technical memorandums, financial statements and filings, engagement working papers, and so on). It is only prudent to reflect current U.S. GAAP in your documentation. The FASB Notice to Constituents (NTC) includes a section on referencing FASB ASC in footnotes and other documents. In this notice, FASB encourages the use of plain English to describe broad topic references in the future. For example, to refer to the requirements of the *Derivatives and Hedging* topic, they suggest a reference similar to "as required by the *Derivatives and Hedging* topic of the FASB *Accounting Standards Codification*." Conversely, FASB suggests using the detailed numerical referencing system in working papers, articles, textbooks, and related items.

.124 Also, because FASB ASC is not intended to change U.S. GAAP, the consistent use of references to only FASB ASC for all periods presented (including periods before the authoritative release of FASB ASC) is appropriate. It is prudent to expect that audit, attest, or compilation and review working papers associated with financial statements for a period ending after September 15, 2009, also would reflect FASB ASC because the underlying financial statements, which are the subjects of those engagements, reference FASB ASC.

.125 However, if your entity will continue to follow grandfathered guidance not included in FASB ASC, it would still be appropriate to reference those standards (and not FASB ASC). A listing of examples of grandfathered guidance can be found in FASB Statement No. 168.

.126 Examples of disclosures using references to FASB ASC can be found at the AICPA's dedicated FASB ASC website at www.aicpa.org/InterestAreas/AccountingAndAuditing/Resources/AcctgFinRptg/AcctgFinRptgGuidance/Pages/FASBAccountingStandardsCodification.aspx.

Decreases in Ownership of a Subsidiary

.127 In January 2010, FASB issued ASU No. 2010-02, *Consolidation (Topic 810): Accounting and Reporting for Decreases in Ownership of a Subsidiary—a Scope Clarification*. This ASU addresses implementation issues related to the changes in ownership provisions in FASB ASC 810-10 (issued as FASB Statement No. 160, *Noncontrolling Interests in Consolidated Financial Statements—an amendment of ARB No. 51*). These amendments clarify that the scope of the decrease in ownership provisions of FASB ASC 810-10 and related guidance applies to a subsidiary or group of assets that is a business or nonprofit activity, a subsidiary that is a business or nonprofit activity that is transferred to an equity method investee or joint venture, and an exchange of a group of assets that constitutes a business or nonprofit activity for a noncontrolling interest in an entity (including an equity method investee or joint venture). Further, the amendments clarify that the decrease in ownership guidance in FASB ASC 810-10 does not apply to the following transactions, even if they involve businesses: sales of in-substance real estate and conveyances of oil and gas mineral rights. The amendment also expands the required disclosures about the deconsolidation of a subsidiary or derecognition of a group of assets within the scope of FASB ASC 810-10. This ASU is effective beginning in the period that an entity adopts FASB Statement No. 160. If an entity has already adopted this guidance, then the amendments in this ASU are effective beginning in the first interim or annual reporting period ending on or after December 15, 2009. The amendments in this ASU should be applied retrospectively to the first period that an entity adopted FASB Statement No. 160.

Accounting for Uncertainty in Income Taxes

.128 For many calendar year nonpublic entities, 2009 was the first year of application of FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes—an interpretation of FASB Statement No. 109*. In September 2009, FASB issued ASU No. 2009-06, *Income Taxes (Topic 740)—Implementation Guidance on Accounting for Uncertainty in Income Taxes and Disclosure Amendments for Nonpublic Entities*. This update affects all nongovernmental entities, and the disclosure amendments only apply to nonpublic entities. The four main provisions of the ASU include the following:

- If income taxes paid by the entity are attributable to the entity, the transaction should be accounted for in accordance with the guidance on uncertainty in income taxes in FASB ASC 740, *Income Taxes*. If the taxes paid by the entity are attributable to the owners, the transaction should be accounted for as a transaction with the owners. Attribution should be based on the laws and regulations of the jurisdiction and should be made for each jurisdiction where the entity is subject to income taxes.
- Management's determination of the taxable status of the entity, including its status as a pass-through entity or tax-exempt NFP,

is a tax position subject to the standards required for accounting for uncertainty in income taxes.

- Regardless of the tax status of the reporting entity, the tax positions of all entities within a related group of entities must be considered.
- For nonpublic entities, it eliminates the disclosures of a tabular reconciliation of the total amount of unrecognized tax benefits at the beginning and end of the periods presented and the total amount of unrecognized tax benefits that, if recognized, would affect the effective tax rate (see FASB ASC 740-10-50-15[a]–[b]).

.129 For entities that are currently applying the guidance on accounting for uncertainty in income taxes, this ASU is effective for interim and annual periods ending after September 15, 2009.

Consolidation of Variable Interest Entities

.130 For calendar year entities, 2010 is the first year of application of FASB Statement No. 167, *Amendments to FASB Interpretation No. 46(R)*, which changes how to determine when an entity that is insufficiently capitalized or is not controlled through voting (or similar rights) should be consolidated. FASB Statement No. 167 was incorporated into FASB ASC through ASU No. 2009-17, *Consolidations (Topic 810): Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities*. This statement is effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009; for interim periods within that first annual reporting period; and for interim and annual reporting periods thereafter. Earlier application is prohibited.

.131 The determination of whether a company is required to consolidate an entity is based on, among other things, an entity's purpose and design and a company's ability to direct the activities of the entity that most significantly impact the entity's economic performance. This statement also amends consolidation of variable interest entities (VIE) guidance to eliminate the quantitative approach previously required for determining the primary beneficiary of a VIE, which was based on determining which enterprise absorbs the majority of the entity's expected losses, receives a majority of the entity's expected residual returns, or both.

.132 Entities will be required to provide additional disclosures about involvement with VIEs and any significant changes in risk exposure due to that involvement. Entities also will be required to disclose how involvement with a VIE affects the entity's financial statements.

.133 FASB Statement No. 167 retains the scope of previous VIE consolidation accounting guidance, with the addition of entities previously considered qualifying special purpose entities because the concept of these entities was eliminated in FASB Statement No. 166, *Accounting for Transfers of Financial Assets—an amendment of FASB Statement No. 140*, which was incorporated into FASB ASC by ASU No. 2009-16, *Transfers and Servicing (Topic 860): Accounting for Transfers of Financial Assets*.

.134 This statement also discusses the objectives of its required disclosures and notes that an entity may need to supplement the minimum required disclosures to meet these objectives. The objectives are for the financial statement users to have an understanding of the following:

- The significant judgments and assumptions made by an enterprise in determining whether it must consolidate a VIE or disclose information about its involvement in a VIE, or both
- The nature of restrictions on a consolidated VIE's assets and on the settlement of its liabilities reported by an enterprise in its statement of financial position, including the carrying amounts of such assets and liabilities
- The nature of, and changes in, the risks associated with an enterprise's involvement with the VIE
- How an enterprise's involvement with the VIE affects the enterprise's financial position, financial performance, and cash flows

Accounting for Transfers of Financial Assets

.135 Calendar year entities must also start applying the provisions of FASB Statement No. 166 in 2010. FASB Statement No. 166, which is a revision to FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities—a replacement of FASB Statement No. 125*, requires more information about transfers of financial assets, including securitization transactions, and those circumstances in which entities have continuing exposure to the risks related to transferred financial assets. FASB Statement No. 166 was incorporated into FASB ASC by ASU No. 2009-16 and is discussed in FASB ASC 860, *Transfers and Servicing*. It eliminates the concept of a qualifying special purpose entity, changes the requirements for derecognizing financial assets, and requires additional disclosures. The purpose of this statement is to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets; the effects of a transfer on its financial position, financial performance, and cash flows; and a transferor's continuing involvement, if any, in transferred financial assets. It is effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009; for interim periods within that first annual reporting period; and for interim and annual reporting periods thereafter. Earlier application is prohibited. This statement must be applied to transfers occurring on or after the effective date; however, the disclosure provisions should be applied to transfers that occurred both before and after the effective date.

.136 Additionally, on and after the effective date, the concept of a qualifying special-purpose entity is no longer relevant for accounting purposes. Therefore, formerly qualifying special purpose entities (as defined under previous accounting standards) should be evaluated for consolidation by reporting entities on and after the effective date in accordance with the applicable consolidation guidance.

.137 The primary objectives of the disclosure requirements of this guidance are to provide the financial statement users with a clear understanding of the following:

- A transferor's continuing involvement (as defined by the FASB ASC glossary), if any, with transferred financial assets
- The nature of any restrictions on assets reported by an entity in its statement of financial position that relate to a transferred financial asset, including the carrying amounts of those assets

- How servicing assets and servicing liabilities are reported under this pronouncement
- For transfers accounted for as sales when a transferor has continuing involvement with the transferred financial assets and for transfers of financial assets accounted for as secured borrowings, how the transfer of financial assets affects a transferor's financial position, financial performance, and cash flows

.138 These objectives must be met by the disclosures, regardless of the specific requirements of the pronouncement. It may be the case that an entity provides greater detail than what is a required disclosure to meet these objectives, depending on the facts and circumstances.

Subsequent Events

.139 FASB Statement No. 165, *Subsequent Events*, which has been codified in FASB ASC 855, *Subsequent Events*, is effective for interim and annual periods ending after June 15, 2009. This statement is intended to establish general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. It requires the disclosure of the date through which an entity has evaluated subsequent events and the basis for that date (that is, whether that date represents the date the financial statements were issued or were available to be issued). The purpose of this disclosure is to alert all users of financial statements that an entity has not evaluated subsequent events after that date in the set of financial statements being presented.

.140 In particular, this statement sets forth the following:

- The period after the balance sheet date during which management of a reporting entity should evaluate events or transactions that may occur for potential recognition or disclosure in the financial statements
- The circumstances under which an entity should recognize events or transactions occurring after the balance sheet date in its financial statements
- The disclosures that an entity should make about events or transactions that occurred after the balance sheet date

.141 FASB states that this guidance should not result in significant changes in current practice with regard to the subsequent events that an entity reports, either through recognition or disclosure, in its financial statements. In September 2009, the AICPA issued Technical Questions and Answers (TIS) section 8700.01, "Effect of FASB ASC 855 on Accounting Guidance in AU Section 560" (AICPA, *Technical Practice Aids*), which notes that preparers of financial statements for nongovernmental entities are required to follow the accounting guidance in FASB ASC 855. Additionally, the accounting guidance contained in AU section 560, *Subsequent Events* (AICPA, *Professional Standards*, vol. 1), would no longer be applicable to audits of nongovernmental entities. This question and answer can be accessed at www.aicpa.org/InterestAreas/AccountingAndAuditing/Resources/Pages/RecentlyIssuedTechnicalQuestionsandAnswers.aspx.

.142 In February 2010, FASB issued ASU No. 2010-09, *Subsequent Events (Topic 855): Amendments to Certain Recognition and Disclosure Requirements*, to address questions that arose in practice about potential conflicts between FASB ASC 855 and SEC guidance—specifically, the requirements to disclose the date that the financial statements are issued. This ASU also addresses the intended breadth of the reissuance disclosure provision related to subsequent events.

.143 ASU No. 2010-09 requires an entity that is an SEC filer or a conduit bond obligor for conduit debt securities that are traded in a public market to evaluate subsequent events through the date the financial statements are issued. All other entities must evaluate subsequent events through the date the financial statements are available to be issued. Further, an entity that is an SEC filer is not required to disclose the date through which subsequent events have been evaluated. Lastly, only non-SEC filers should disclose in the revised financial statements the dates through which subsequent events have been evaluated in both the issued or available-to-be-issued financial statements and the revised financial statements. Revised financial statements are considered reissued financial statements.

.144 The amendments in ASU No. 2010-09 are effective upon issuance, except for the use of the issued date for conduit bond obligors. That amendment is effective for interim or annual periods ending after June 15, 2010. In June 2010, the AICPA issued TIS section 8700.03, "Auditor's Responsibilities for Subsequent Events Relative to a Conduit Debt Obligor" (AICPA, *Technical Practice Aids*), to provide guidance related to the effect of this ASU on the auditor's responsibilities for subsequent events relative to a conduit debt obligor and the date of the auditor's report.

Fair Value

.145 FASB ASC 820-10-20 defines *fair value* and establishes a framework for measuring fair value; however, it does not dictate when an entity must measure something at fair value, nor does it expand the use of fair value in any way. The need to understand fair value accounting has increased in importance as alternative investments increased in popularity and complexity. *Fair value* is defined as "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date."

Measuring Liabilities at Fair Value

.146 FASB issued ASU No. 2009-05, *Measuring Liabilities at Fair Value*, to increase the consistency in the application of FASB ASC 820 to liabilities because many constituents had expressed concern. This ASU applies to all entities that measure liabilities at fair value under FASB ASC 820 and amends sections of FASB ASC 820-10.

.147 This ASU states that, in circumstances in which a quoted price in an active market for the identical liability is not available, fair value of the liability must be measured by either (*a*) a valuation technique that uses the quoted price of the identical liability when traded as an asset or quoted prices for similar liabilities, or similar liabilities when traded as assets, or (*b*) another valuation technique that is consistent with the principles of FASB ASC 820, such as an income approach or a market approach. Further, if a restriction on the transference of the liability exists, the ASU clarifies that an entity is not required to factor that in to the inputs of the fair value determination. Lastly, the ASU also clarifies that a quoted price in an active market for the identical liability, or an unadjusted quoted price in an active market for the identical liability, when traded as an asset, are level 1 measurements within the fair value hierarchy. The guidance in this ASU is effective for the first reporting period (including interim periods) beginning after its issuance in August 2009. The full text of the ASU can be accessed from FASB's website at www.fasb.org.

Investments in Certain Entities That Calculate Net Asset Value per Share (or its Equivalent)

.148 FASB issued ASU No. 2009-12, *Fair Value Measurements and Disclosures (Topic 820): Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*, because of the complexities and practical difficulties in estimating the fair value of alternative investments. It is applicable to all reporting entities that hold an investment that is required or permitted to be measured or disclosed at fair value on a recurring or nonrecurring basis, and as of the reporting entity's measurement date, if the investment both

- does not have a *readily determinable fair value*. The FASB ASC glossary states that an equity security has a readily determinable fair value if it meets any of the following conditions:
  - — The fair value of any equity security is readily determinable if sales prices or bid-and-asked quotations are currently available on a securities exchange registered with the SEC or in the over-the-counter (OTC) market, provided that those prices or quotations for the OTC market are publicly reported by NASDAQ or by Pink Sheets LLC. Restricted stock meets that definition if the restriction terminates within one year.
  - — The fair value of an equity security traded only in a foreign market is readily determinable if that foreign market is of a breadth and scope comparable to one of the U.S. markets referred to previously.
  - — The fair value of an investment in a mutual fund is readily determinable if the fair value per share (unit) is determined and published and is the basis for current transactions.
- is in an entity that has all of the attributes specified in FASB ASC 946-10-15-2 or, if one of those attributes are not met, is in an entity for which it is industry practice to issue financial statements using guidance that is consistent with the measurement principles in FASB ASC 946, *Financial Services—Investment Companies*.

.149 As a practical expedient, this ASU permits a reporting entity to measure the fair value of an investment within its scope on the basis of the net asset value (NAV) per share of the investment (or its equivalent) if the NAV is calculated in a manner consistent with the measurement principles of FASB ASC 946 as of the reporting entity's measurement date, including measurement of all or substantially all of the underlying investments of the investee in accordance with FASB ASC 820. If the practical expedient is used, certain attributes of the investment (such as restrictions on redemption) and transaction prices from principal-to-principal or brokered transactions will not be considered in measuring the investment's fair value.

.150 This ASU also requires disclosures by major category of investment about the attributes of investments, such as the nature of any restrictions on the investor's ability to redeem its investments at the measurement date, any unfunded commitments, and the investment strategies of the investees. The major category of investment is required to be determined based on the guidance in FASB ASC 320-10-50-1B. These disclosures are required for all investments within the scope of this ASU regardless of whether the practical expedient has been applied. The ASU adds an example of its required disclosures in FASB ASC 820-10-55-64A.

.151 These amendments are effective for interim and annual periods ending after December 15, 2009 and are included in FASB ASC 820-10. An AICPA practice aid, *Alternative Investments—Audit Considerations*, also is available and is a useful tool for auditors. It focuses on the existence and valuation assertions associated with alternative investments.

.152 In December 2009, the AICPA issued sections .18–.27 of TIS section 2220, *Long-Term Investments* (AICPA, *Technical Practice Aids*), to assist reporting entities when implementing the provisions of FASB ASC 820 to estimate the fair value of their investments in certain entities that calculate NAV. TIS sections 2220.18–.27 apply to investments that are required to be measured and reported at fair value and are within the scope of paragraphs 4–5 of FASB ASC 820-10-15. These questions and answers compliment the guidance provided in ASU No. 2009-12.

.153 Topics covered in these questions and answers include the following:

- The circumstances when NAV may be used to estimate the fair value of investments as a practical expedient
- How to identify the unit of account for interests in alternative investments
- Considerations for determining whether the reported NAV has been calculated in a manner consistent with FASB ASC 946
- Examples of circumstances when an adjustment to the reported NAV may be necessary
- How to adjust the reported NAV when it is not as of the reporting entity's measurement date
- How to adjust the reported NAV when it has not been calculated in accordance with FASB ASC 946
- The determination of the appropriate level within the fair value hierarchy for NAV of alternative investments in relation to the ability to redeem the investment versus the actual redemption request for the investment
- The definition of *near term* for the purposes of determining the appropriate level within the fair value hierarchy
- The tailoring of disclosures categories to address the nature and risks of investments
- Some considerations for determining the fair value of alternative investments when not utilizing NAV as a practical expedient

.154 Recently issued questions and answers can be located on the AICPA website at www.aicpa.org/InterestAreas/AccountingAndAuditing/Resources/Pages/RecentlyIssuedTechnicalQuestionsandAnswers.aspx.

Fair Value Measurements Disclosures

.155 ASU No. 2010-06, *Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements*, was issued to increase the transparency in financial reporting of fair value measurements. FASB noted that due to the different degrees of subjectivity and reliability on level 1, level 2, and level 3 fair value measurements, information about significant transfers between the three levels and the underlying reasons for such transfers would be useful to financial statements users.

.156 This ASU amends FASB ASC 820-10 to require the following new disclosures:

- *Transfers in and out of levels 1 and 2*. A reporting entity should disclose separately the amounts of significant transfers in and out of level 1 and level 2 fair value measurements and describe the reasons for the transfers.
- *Activity in level 3 fair value measurements*. In the reconciliation for fair value measurements using significant unobservable inputs (level 3), a reporting entity should present separately information about purchases, sales, issuances, and settlements (that is, on a gross basis rather than as one net number).

.157 Additionally, the ASU amends FASB ASC 820-10 to clarify certain existing disclosures as follows:

- *Level of disaggregation*. A reporting entity should provide fair value measurement disclosures for each class of assets and liabilities. A class is often a subset of assets or liabilities within a line item in the statement of financial position. A reporting entity needs to use judgment in determining the appropriate classes of assets and liabilities.
- *Disclosures about inputs and valuation techniques*. A reporting entity should provide disclosures about the valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements. Those disclosures are required for fair value measurements that fall in either level 2 or level 3.

.158 The amendments in ASU No. 2010-06 are effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances, and settlements in the rollforward of activity in level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years.

Disclosures About Credit Quality and Allowance for Credit Losses

.159 In July 2010, FASB issued ASU No. 2010-20, *Receivables (Topic 310): Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses*, which requires an entity to provide a greater level of disaggregated information about the credit quality of its financing receivables and its allowance for credit losses. The ASU amends the existing disclosures to require an entity to provide the following disclosures about its financing receivables on a disaggregated basis:

- A rollforward schedule of the allowance for credit losses from the beginning of the reporting period to the end of the reporting period on a portfolio segment basis, with the ending balance further disaggregated on the basis of the impairment method. For each disaggregated ending balance, the related recorded investment in financing receivables should also be disclosed.
- The nonaccrual status of financing receivables by class of financing receivables.
- Impaired financing receivables by class of financing receivables.

.160 The amendments in this ASU require an entity to provide the following additional disclosures about its financing receivables:

- Credit quality indicators of financing receivables at the end of the reporting period by class of financing receivables (see FASB ASC 310-10-55-19 for examples of credit quality indicators)
- The aging of past due financing receivables at the end of the reporting period by class of financing receivables
- The nature and extent of troubled debt restructurings that occurred during the period by class of financing receivables and their effect on the allowance for credit losses
- The nature and extent of financing receivables modified as troubled debt restructurings within the previous 12 months that defaulted during the reporting period by class of financing receivables and their effect on the allowance for credit losses
- Significant purchases and sales of financing receivables during the reporting period disaggregated by portfolio segment

.161 An entity must also describe, by portfolio segment, its accounting policies and methodology used to estimate its allowance for credit losses, including the identification of any changes to the entity's accounting policies or methodology from the prior period and the entity's rationale for the change.

.162 The amendments in this ASU apply to all entities with financing receivables. Examples of financing receivables include loans; trade receivables; notes receivable; and receivables relating to a lessor's leveraged, direct financing, and sales-type leases. See the "Pending Content" in paragraphs 13–15 of FASB ASC 310-10-55 for more information on the definition of *financing receivable*, including a list of items that are excluded from the definition (for example, debt securities). In addition, the "Pending Content" in paragraphs 7–12 of FASB ASC 310-10-55 illustrates certain disclosures required by this ASU.

.163 For public entities, the disclosures as of the end of a reporting period are effective for interim and annual reporting periods ending on or after December 15, 2010. The disclosures about activity that occurs during a reporting period are effective for interim and annual reporting periods beginning on or after December 15, 2010. For nonpublic entities, the disclosures are effective for annual reporting periods ending on or after December 15, 2011.

Recently Issued GASB Pronouncements and Related Guidance

.164 The following summaries are for informational purposes only and should not be relied upon as a substitute for a complete reading of the applicable standard.

GASB Statement No. 58, Accounting and Financial Reporting for Chapter 9 Bankruptcies

.165 The objective of GASB Statement No. 58, which was issued in December 2009 and is effective for reporting periods beginning after June 15, 2009, is to provide accounting and financial reporting guidance for governments that have petitioned for protection from creditors by filing for bankruptcy under Chapter 9 of the U.S. Bankruptcy Code. It requires governments to remeasure liabilities that are adjusted in bankruptcy when the bankruptcy court confirms (that is, approves) a new payment plan.

.166 For accounts payable, notes, debentures and bonds, and related interest payable, this statement requires governments to base remeasurement on the new payment plan. Reductions in future interest payments would result in lower interest costs reported in future periods. Reductions to principal or accrued interest payable may result in gains reported at the time of the reduction. If the new payment plan does not indicate whether it reduces principal payments or future interest payments that have not been accrued, the debt should be remeasured at the present value of the future payments using the original discount rate, and a gain should be reported at the time of the reduction.

.167 For leases, pollution remediation liabilities, and liabilities for pension and other postemployment benefit plans, this statement requires remeasurement based on existing authoritative guidance. However, if a benefit plan is rejected in bankruptcy and becomes general unsecured debt, GASB Statement No. 58 requires the existing liability to be removed and a new approved payment plan to be recognized as a judgment, with a gain or loss recognized for the difference. Gains or losses resulting from remeasurement of liabilities and assets should be classified as an extraordinary item.

.168 For governments that are not expected to emerge from bankruptcy as going concerns, this statement requires remeasurement of assets to a value that represents the amount expected to be received.

.169 Governments that have filed for bankruptcy are required to disclose information regarding, among other things, the pertinent conditions and events giving rise to the petition for bankruptcy, the expected gain, and the effects upon services.

GASB Statement No. 57, OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans

.170 Issued in December 2009, GASB Statement No. 57 addresses issues related to the use of the alternative measurement method and the frequency and timing of measurements by employers that participate in agent multiple-employer other postemployment benefit (OPEB) plans (that is, agent employers).

.171 This statement amends GASB Statement No. 45, *Accounting and Financial Reporting by Employers to Postemployment Benefits Other Than Pensions*, to permit an agent employer that has an individual-employer OPEB plan with fewer than 100 total plan members to use the alternative measurement method at its option, regardless of the number of total plan members in the agent multiple-employer OPEB plan in which it participates. Consistent with this change to the employer-reporting requirements, this statement also amends a GASB Statement No. 43, *Financial Reporting for Postemployment*

Benefit Plans Other Than Pension Plans, requirement that a defined benefit OPEB plan obtain an actuarial valuation. The amendment permits the requirement to be satisfied for an agent multiple-employer OPEB plan by reporting an aggregation of results of actuarial valuations of the individual-employer OPEB plans or measurements resulting from the use of the alternative measurement method for individual-employer OPEB plans that are eligible.

.172 In addition, GASB Statement No. 57 clarifies that when actuarially determined OPEB measures are reported by an agent multiple-employer OPEB plan and its participating employers, those measures should be determined as of a common date and at a minimum frequency to satisfy the agent multiple-employer OPEB plan's financial reporting requirements.

.173 The provisions related to the use and reporting of the alternative measurement method are effective upon issuance. The provisions related to the frequency and timing of measurements are effective for actuarial valuations first used to report funded status information in OPEB plan financial statements for periods beginning after June 15, 2011.

Convergence With International Financial Reporting Standards

.174 Since the signing of the Norwalk Agreement by FASB and the International Accounting Standards Board (IASB), the bodies have had a common goal—one set of accounting standards for international use. *International convergence of accounting standards* refers to both the goal of this project and the path taken to reach it. The path toward reaching this goal will both improve U.S. GAAP and International Financial Reporting Standards (IFRSs) and eliminate the differences between them. In the Norwalk agreement, each body acknowledged its commitment to the development of high quality, compatible accounting standards that could be used for both domestic and cross-border financial reporting. FASB and the IASB have undertaken several joint projects, which are being conducted simultaneously in a coordinated manner to further the goal of convergence of U.S. GAAP and IFRSs. The "On the Horizon" section of this alert discusses these joint projects. For more information, visit www.fasb.org and www.iasb.org.

SEC Work Plan for Consideration of IFRSs

.175 In February 2010, the SEC issued Release No. 33-9109, *Commission Statement in Support of Convergence and Global Accounting Standards*. This release provides an update to the SEC's roadmap on its consideration of global accounting standards, including a confirmation of its continued support for the convergence of U.S. GAAP and IFRSs in order to narrow the differences between the two sets of standards. The SEC believes that a more comprehensive work plan is necessary to transparently lay out the work that must be done to support a decision on the appropriate course to incorporate IFRSs into the U.S. financial reporting system for U.S. issuers, including the scope, time frame, and methodology for any such transition. Therefore, the SEC has indicated that it will carefully consider and deliberate whether these changes are in the best interest of U.S. investors and markets.

.176 The SEC directed its staff to execute a work plan, the results of which will aid the SEC in its evaluation of the impact that the use of IFRSs by U.S. entities would have on the U.S. securities market. The work plan includes consideration of IFRSs, both as they currently exist and after the completion of the various convergence projects underway by FASB and the IASB. Among other things, the work plan addresses some of the comments and concerns received on the roadmap, including the following:

- Sufficient development and application of IFRSs for the U.S. reporting system
- The independence of standard setting for the benefit of investors
- Investor understanding and education regarding IFRSs
- Examination of the U.S. regulatory environment that would be affected by a change in accounting standards
- The impact on issuers, both large and small, including changes to accounting systems, changes to contractual arrangements, corporate governance considerations, and litigation contingencies
- Human capital readiness

.177 Beginning no later than October 2010, and frequently thereafter, the SEC staff will provide public progress reports on the work plan, as well as the status of the FASB and IASB convergence projects, until the work is complete. By 2011, assuming completion of these convergence projects and the staff's work plan, the SEC will decide whether to incorporate IFRSs into the U.S. financial reporting system and, if so, when and how. Commentors provided feedback on the timing discussed in the roadmap, suggesting that a four or five year time frame would be necessary to successfully implement a change in their financial reporting systems to incorporate IFRSs. Under that assumption, if the SEC determines in 2011 to incorporate IFRSs into the U.S. financial reporting system, the first time that U.S. entities would report under such a system would be no earlier than 2015. This timeline will be further evaluated as part of the work plan. The work plan is included as an appendix at the end of Release No. 33-9109 and also can be found on the SEC's website at www.sec.gov.

.178 In August 2010, the SEC issued two releases (Release Nos. 33-9133 and 33-9134, Notice of Solicitation of Public Comment on Consideration of Incorporating IFRS Into the Financial Reporting System for U.S. Issuers) to solicit public comment on its ongoing consideration of incorporating IFRSs into the financial reporting system for U.S. issuers. The first release contains requests for comment on three topics derived from the work plan that are related to the potential impact on investors. The second release contains requests for comment on three topics, also derived from the work plan, that are related to the potential impact on U.S. issuers. All comments will be available on the SEC's website.

International Financial Reporting Standard for Small and Medium-sized Entities

.179 The IASB issued *International Financial Reporting Standard for Small and Medium-sized Entities* (*IFRS for SMEs*) to be a self-contained global accounting and financial reporting standard applicable to the general purpose financial statements of, and other financial reporting by, entities that are known in many countries as SMEs. *IFRS for SMEs* is intended to be used by entities that publish general purpose financial statements for external users and do not have public accountability.

.180 The AICPA Governing Council recognizes the IASB as an accounting body for purposes of establishing international financial accounting and reporting principles. This amendment to appendix A of AICPA Rule 202, *Compliance*

With Standards (AICPA, *Professional Standards*, vol. 2, ET sec. 202 par. .01), and Rule 203, *Accounting Principles* (AICPA, *Professional Standards*, vol. 2, ET sec. 203 par. .01), gives AICPA members the option to use IFRSs as an alternative to U.S. GAAP. As such, a key professional barrier to using IFRSs and, therefore, *IFRS for SMEs* has been removed. CPAs may need to check with their state boards of accountancy to determine the status of reporting on financial statements prepared in accordance with *IFRS for SMEs* within their individual state. Any remaining barriers may come in the form of unwillingness by a private company's financial statement users to accept financial statements prepared under *IFRS for SMEs*, and a private company's expenditure of money, time and effort to convert to *IFRS for SMEs*.

.181 Information about IFRSs and *IFRS for SMEs* can be found at www.ifrs.com. Additionally, to help its membership, the AICPA has developed an IFRS for SMEs—U.S. GAAP Comparison Wiki. The purpose of the Wiki is to provide a detailed and comprehensive comparison of *IFRS for SMEs* with corresponding requirements of U.S. GAAP. But it is more than just a comparison resource—it is a wiki. That means it is a collaborative, ongoing work in progress for anyone to contribute to and use. The Wiki is found at http://wiki.ifrs.com/.

.182 Entities interested in IFRS for SMEs or possibly adopting the standard may find it helpful to take the following actions:

- *Monitor the efforts of the AICPA/FAF/NASBA "Blue-Ribbon" Panel on Standard Setting for Private Companies*. For more information about the panel, go to www.fasb.org/cs/ContentServer?c=Page&pagename=FASB%2FPage%2FSectionPage&cid=1176156684820.
- *Monitor convergence efforts of FASB and the IASB*.
- *Stay informed on SEC developments*. Public companies will be directly affected by the SEC's decision to adopt IASB standards. The future of private company reporting will also likely be affected by an SEC mandate to adopt IFRSs.
- *Develop a high-level analysis of the potential impact on accounting policies, processes and systems, contracts, legal agreements, and financing and tax structures*.

Private Company Financial Reporting

.183 The AICPA and the Financial Accounting Foundation established the "blue-ribbon panel" to address how U.S. accounting standards can best meet the needs of U.S. users of private company financial statements. This panel also is sponsored by the National Association of State Boards of Accountancy. The "blue-ribbon panel" will provide recommendations through an issued report on the future of standard setting for private companies, including whether separate, stand-alone accounting standards for private companies are needed. The panel has discussed how smaller entities are struggling to understand and implement complex standards, which has resulted in entities taking more GAAP exceptions. Other key items include (*a*) whether U.S. GAAP is meeting private company user needs in a cost-beneficial manner for both users and preparers, (*b*) how private company standard setting in the United States compares to standard setting in other countries, and (*c*) possible lessons to be learned from alternatives seen in other countries. The panel's issued report will be made available to the public, and the resulting action plan is expected to be exposed for public comment prior to that plan being finalized. The panel will issue a report containing its recommendations to the Financial Accounting Foundation (FAF) board of trustees in January 2011. The report will be publicly available, and the resulting action plan is expected to be exposed for public comment prior to the plan being finalized.

.184 During the July 2010 meeting of the panel, seven alternative models for private company financial reporting were discussed. Models based on IFRSs and a model that would have resulted in no change to private company financial reporting were eliminated. All remaining models would result in differences in GAAP for private and public entities; the main focus of the panel moving forward will be to select a model that is relevant to users of private company financial reports because this has become the overriding issue. The three primary models the panel agreed to focus on going forward are U.S. GAAP with Exclusions for Private Companies—with enhancements; U.S. GAAP—Baseline GAAP with Public Company Add-Ons; and Separate, Stand-Alone GAAP Based on Current U.S. GAAP. Most of the panel members also expressed their discontent with the current make-up of FASB and its heavy, but appropriate, focus on public companies. This led to another key discussion topic: the structure of whatever model is chosen—the current FASB; a restructured FASB (with greater private company representation); or a new, separate Private Company Standards Board under the oversight of FAF.

Recent Pronouncements

.185 AICPA auditing and attestation standards are applicable only to audits and attestation engagements of nonissuers. The PCAOB establishes auditing and attestation standards for audits of issuers. For information on pronouncements issued subsequent to the writing of this alert, please refer to the AICPA website at www.aicpa.org, the FASB website at www.fasb.org, and the PCAOB website at www.pcaob.org. You also may look for announcements of newly issued accounting standards in the *CPA Letter Daily* and the *Journal of Accountancy*.

Recent Auditing and Attestation Pronouncements and Related Guidance

.186 The following table presents a list of recently issued audit and attestation pronouncements and related guidance.

Recent Auditing and Attestation Pronouncements and Related Guidance

Statement on Auditing Standards (SAS) No. 120, *Required Supplementary Information* (AICPA, *Professional Standards*, vol. 1, AU sec. 558) Issue Date: February 2010 (Applicable to audits conducted in accordance with generally accepted auditing standards [GAAS])	This standard addresses the auditor's responsibility with respect to information that a designated accounting standard setter requires to accompany an entity's basic financial statements. In the absence of any separate requirement in the particular circumstances of the engagement, the auditor's opinion on the basic financial statements does not cover required supplementary information. It also supersedes AU section 558, *Required Supplementary Information* (AICPA, *Professional Standards*, vol. 1). This SAS is effective for periods beginning on or after December 15, 2010. Early application is permitted.
SAS No. 119, *Supplementary Information in Relation to the Financial Statements as a Whole* (AICPA, *Professional Standards*, vol. 1, AU sec. 551) Issue Date: February 2010 (Applicable to audits conducted in accordance with GAAS)	This SAS addresses the auditor's responsibility when engaged to report on whether supplementary information is fairly stated, in all material respects, in relation to the financial statements as a whole. The information covered by this SAS is presented outside the basic financial statements and is not considered necessary for the financial statements to be fairly presented in accordance with the applicable financial reporting framework. Along with SAS No. 118, *Other Information in Documents Containing Audited Financial Statements* (AICPA, *Professional Standards*, vol. 1, AU sec. 550), this SAS also supersedes AU section 551A, *Reporting on Information Accompanying the Basic Financial Statements in Auditor-Submitted Documents* (AICPA, *Professional Standards*, vol. 1). This SAS is effective for periods beginning on or after December 15, 2010. Early application is permitted.

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Recent Auditing and Attestation Pronouncements and Related Guidance	
SAS No. 118, *Other Information in Documents Containing Audited Financial Statements* (AICPA, *Professional Standards*, vol. 1, AU sec. 550) Issue Date: February 2010 (Applicable to audits conducted in accordance with GAAS)	This SAS addresses the auditor's responsibility in relation to other information in documents containing audited financial statements and the auditor's report thereon. In the absence of any separate requirement in the particular circumstances of the engagement, the auditor's opinion on the financial statements does not cover other information, and the auditor has no responsibility for determining whether such information is properly stated. This SAS establishes the requirement for the auditor to read the other information of which the auditor is aware because the credibility of the audited financial statements may be undermined by material inconsistencies between the audited financial statements and other information. This SAS supersedes AU section 550A, *Other Information in Documents Containing Audited Financial Statements* (AICPA, *Professional Standards*, vol. 1), and along with SAS No. 119, supersedes AU section 551A. This SAS is effective for periods beginning on or after December 15, 2010. Early application is permitted.
SAS No. 117, *Compliance Audits* (AICPA, *Professional Standards*, vol. 1, AU sec. 801) Issue Date: December 2009 (Applicable to audits conducted in accordance with GAAS)	This standard amends AU section 801 to reflect changes in the compliance audit environment and incorporates the risk assessment standards. It requires the auditor to adapt and apply the AU sections of the AICPA's *Professional Standards* to compliance audits and provides guidance on how to do so. It is effective for compliance audits for fiscal periods ending on or after June 15, 2010. Earlier application is permitted.

Recent Auditing and Attestation Pronouncements and Related Guidance	
SAS No. 115, *Communicating Internal Control Related Matters Identified in an Audit* (AICPA, *Professional Standards*, vol. 1, AU sec. 325) Issue Date: October 2008 (Applicable to audits conducted in accordance with GAAS)	Replacing SAS No. 112, *Communicating Internal Control Related Matters Identified in an Audit*, this standard defines the terms *deficiency in internal control*, *significant deficiency*, and *material weakness*; provides guidance on evaluating the severity of deficiencies in internal control identified in an audit of financial statements; and requires the auditor to communicate in writing to management and those charged with governance significant deficiencies and material weaknesses identified in an audit. It is effective for audits of financial statements for periods ending on or after December 15, 2009. Earlier implementation is permitted.
Statement on Standards for Attestation Engagements (SSAE) No. 16, *Reporting on Controls at a Service Organization* (AICPA, *Professional Standards*, vol. 1, AT sec. 801) Issue Date: April 2010	SSAE No. 16 supersedes the guidance for service auditors in AU section 324, *Service Organizations* (AICPA, *Professional Standards*, vol. 1), and addresses examination engagements undertaken by a service auditor to report on controls at organizations that provide services to user entities when those controls are likely to be relevant to user entities' internal control over financial reporting. Reports prepared in accordance with SSAE No. 16 may provide appropriate evidence under AU section 324. It is effective for service auditors' reports for periods ending on or after June 15, 2011. Earlier implementation is permitted.
Public Company Accounting Oversight Board (PCAOB) Auditing Standard No. 15, *Audit Evidence* (subject to approval by the Securities and Exchange Commission [SEC]) Issue Date: August 2010 (Applicable to audits conducted in accordance with PCAOB standards)	This standard explains what constitutes audit evidence and establishes requirements for designing and performing audit procedures to obtain sufficient appropriate audit evidence to support the opinion expressed in the auditor's report.

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Recent Auditing and Attestation Pronouncements and Related Guidance	
PCAOB Auditing Standard No. 14, *Evaluating Audit Results* (subject to approval by the SEC) Issue Date: August 2010 (Applicable to audits conducted in accordance with PCAOB standards)	This standard establishes requirements regarding the auditor's evaluation of audit results and determination of whether the auditor has obtained sufficient appropriate audit evidence. The evaluation process set forth in this standard includes, among other things, evaluation of misstatements identified during the audit; the overall presentation of the financial statements, including disclosures; and the potential for management bias in the financial statements.
PCAOB Auditing Standard No. 13, *The Auditor's Responses to the Risks of Material Misstatement* (subject to approval by the SEC) Issue Date: August 2010 (Applicable to audits conducted in accordance with PCAOB standards)	This standard establishes requirements for responding to the risks of material misstatement in financial statements through the general conduct of the audit and performing audit procedures regarding significant accounts and disclosures.
PCAOB Auditing Standard No. 12, *Identifying and Assessing Risks of Material Misstatement* (subject to approval by the SEC) Issue Date: August 2010 (Applicable to audits conducted in accordance with PCAOB standards)	This standard establishes requirements regarding the process of identifying and assessing risks of material misstatement of the financial statements. The risk assessment process discussed in the standard includes information-gathering procedures to identify risks and an analysis of the identified risks.
PCAOB Auditing Standard No. 11, *Consideration of Materiality in Planning and Performing an Audit* (subject to approval by the SEC) Issue Date: August 2010 (Applicable to audits conducted in accordance with PCAOB standards)	This standard describes the auditor's responsibilities for consideration of materiality in planning and performing an audit.
PCAOB Auditing Standard No. 10, *Supervision of the Audit Engagement* (subject to approval by the SEC) Issue Date: August 2010 (Applicable to audits conducted in accordance with PCAOB standards)	This standard sets forth requirements for supervision of the audit engagement, including, in particular, supervising the work of engagement team members. It applies to the engagement partner and to other engagement team members who assist the engagement partner with supervision.

Recent Auditing and Attestation Pronouncements and Related Guidance

PCAOB Auditing Standard No. 9, *Audit Planning* (subject to approval by the SEC) Issue Date: August 2010 (Applicable to audits conducted in accordance with PCAOB standards)	This standard establishes requirements regarding planning an audit, including assessing matters that are important to the audit, and establishing an appropriate audit strategy and audit plan.
PCAOB Auditing Standard No. 8, *Audit Risk* (subject to approval by the SEC) Issue Date: August 2010 (Applicable to audits conducted in accordance with PCAOB standards)	This standard discusses the auditor's consideration of audit risk in an audit of financial statements as part of an integrated audit or an audit of financial statements only. It describes the components of audit risk and the auditor's responsibilities for reducing audit risk to an appropriately low level in order to obtain reasonable assurance that the financial statements are free of material misstatement.
PCAOB Auditing Standard No. 7, *Engagement Quality Review* (AICPA, *PCAOB Standards and Related Rules*, Standards, AU-P sec.162) Issue Date: January 2010 (Applicable to audits conducted in accordance with PCAOB standards)	This standard and its related amendments supersede the interim concurring partner review requirements and update the interim quality control standards. An engagement quality review and concurring approval of issuance are required for each audit engagement and for each engagement to review interim financial information conducted pursuant to the standards of the PCAOB. The standard provides a framework for the engagement quality reviewer to objectively evaluate the significant judgments made and related conclusions reached by the engagement team in forming an overall conclusion about the engagement. It is effective for engagement quality reviews of audits and interim reviews for fiscal years that began on or after December 15, 2009.

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Recent Auditing and Attestation Pronouncements and Related Guidance	
PCAOB Staff Question and Answer, *Auditing Standard No. 7,* Engagement Quality Review (AICPA, *PCAOB Standards and Related Rules*, PCAOB Staff Guidance, sec. 100.10) Issue Date: February 2010 (Applicable to audits conducted in accordance with PCAOB standards),	This staff question and answer provides further implementation guidance on the documentation requirements of Auditing Standard No. 7 (AU-P sec. 162) in light of comments the SEC received during its comment period.
PCAOB Staff Audit Practice Alert No. 6, *Auditor Considerations Regarding Using the Work of Other Auditors and Engaging Assistants from Outside the Firm* (AICPA, *PCAOB Standards and Related Rules*, PCAOB Staff Guidance, sec. 400.06) Issue Date: July 2010 (Applicable to audits conducted in accordance with PCAOB standards)	This alert is intended to remind registered public accounting firms of their obligations when using the work of other firms or using assistants engaged from outside the firm. The alert was prompted by observations by the PCAOB that a number of registered public accounting firms located within the United States have been issuing reports on financial statements filed by issuers that have substantially all of their operations outside of the United States, and some of these firms may not be conducting those audits in accordance with PCAOB standards.
PCAOB Staff Audit Practice Alert No. 5, *Auditor Considerations Regarding Significant Unusual Transactions* (AICPA, *PCAOB Standards and Related Rules*, PCAOB Staff Guidance, sec. 400.05) Issue Date: April 2010 (Applicable to audits conducted in accordance with PCAOB standards)	This alert explains that significant unusual transactions, especially those close to period-end that pose difficult substance over form questions, can provide opportunities for entities to engage in fraudulent financial reporting. This staff audit practice alert is designed to remind auditors of public companies about their responsibilities to assess and respond to the risk of material misstatement of the financial statements due to error or fraud posed by significant unusual transactions.

Recent ASUs

.187 The following table presents, by codification area, a list of recently issued ASUs, through the issuance of ASU No. 2010-24. However, this table does not include ASUs that are SEC updates (such as ASU No. 2010-19, *Foreign Currency [Topic 830]: Foreign Currency Issues: Multiple Foreign Currency Exchange Rates [SEC Update]*) or ASUs that are technical corrections to various topics. FASB ASC does include SEC content to improve the usefulness of FASB ASC for public companies, but the content labeled as SEC staff guidance does not constitute rules or interpretations of the SEC nor does such guidance bear official SEC approval.

Recent Accounting Standards Updates	
Assets Area of Financial Accounting Standards Board (FASB) *Accounting Standards Codification* (ASC)	
Accounting Standards Update (ASU) No. 2010-20 (July 2010)	*Receivables (Topic 310): Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses*
ASU No. 2010-18 (April 2010)	*Receivables (Topic 310): Effect of a Loan Modification When the Loan Is Part of a Pool That Is Accounted for as a Single Asset—a consensus of the FASB Emerging Issues Task Force*
Liabilities Area of FASB ASC	
ASU No. 2009-15 (October 2009)	*Accounting for Own-Share Lending Arrangements in Contemplation of Convertible Debt Issuance or Other Financing—a consensus of the FASB Emerging Issues Task Force*
Equity Area of FASB ASC	
ASU No. 2010-01 (January 2010)	*Equity (Topic 505): Accounting for Distributions to Shareholders with Components of Stock and Cash—a consensus of the FASB Emerging Issues Task Force*
Revenue Area of FASB ASC	
ASU No. 2010-17 (April 2010)	*Revenue Recognition—Milestone Method (Topic 605): Milestone Method of Revenue Recognition—a consensus of the FASB Emerging Issues Task Force*
ASU No. 2009-13 (October 2009)	*Revenue Recognition (Topic 605): Multiple-Deliverable Revenue Arrangements—a consensus of the FASB Emerging Issues Task Force*
Expenses Area of FASB ASC	
ASU No. 2010-13 (April 2010)	*Compensation—Stock Compensation (Topic 718): Effect of Denominating the Exercise Price of a Share-Based Payment Award in the Currency of the Market in Which the Underlying Equity Security Trades—a consensus of the FASB Emerging Issues Task Force*

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Recent Accounting Standards Updates	
Broad Transactions Area of FASB ASC	
ASU No. 2010-10 (February 2010)	*Consolidation (Topic 810): Amendments for Certain Investment Funds*
ASU No. 2010-02 (January 2010)	*Consolidation (Topic 810): Accounting and Reporting for Decreases in Ownership of a Subsidiary—a Scope Clarification*
ASU No. 2009-17 (December 2009)	*Consolidations (Topic 810): Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities*
ASU No. 2010-11 (March 2010)	*Derivatives and Hedging (Topic 815): Scope Exception Related to Embedded Credit Derivatives*
ASU No. 2010-06 (January 2010)	*Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements*
ASU No. 2009-12 (September 2009)	*Fair Value Measurements and Disclosures (Topic 820): Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*
ASU No. 2010-09 (February 2010)	*Subsequent Events (Topic 855): Amendments to Certain Recognition and Disclosure Requirements*
ASU No. 2009-16 (December 2009)	*Transfers and Servicing (Topic 860): Accounting for Transfers of Financial assets*
Industry Area of FASB ASC	
ASU No. 2010-24 (August 2010)	*Health Care Entities (Topic 954): Presentation of Insurance Claims and Related Insurance Recoveries (a consensus of the FASB Emerging Issues Task Force)*
ASU No. 2010-23 (August 2010)	*Health Care Entities (Topic 954): Measuring Charity Care for Disclosure—a consensus of the FASB Emerging Issues Task Force*
ASU No. 2010-07 (January 2010)	*Not-for-Profit Entities (Topic 958): Not-for-Profit Entities: Mergers and Acquisitions*

Recently Issued Technical Questions and Answers

.188 The following table presents a list of nonauthoritative accounting and audit and attest technical questions and answers recently issued by the AICPA. Recently issued questions and answers can be accessed at www.aicpa.org/InterestAreas/AccountingAndAuditing/Resources/Pages/RecentlyIssuedTechnicalQuestionsandAnswers.aspx.

Recently Issued Technical Questions and Answers (AICPA, *Technical Practice Aids*)	
Accounting	
Technical Questions and Answers (TIS) section 6931.12 (July 2010)	"Accounting and Disclosure Requirements for Health and Welfare Plans Related to the COBRA Premium Subsidy Included in the American Recovery and Reinvestment Act of 2009"
TIS section 9070.06 (June 2010)	"Decline in Market Value of Assets Subsequent to the Balance Sheet Date"
TIS section 6140.25 (June 2010)	"Multiyear Unconditional Promises to Give—Measurement Objective and the Effect of Changes in Interest Rates"
TIS section 6140.24 (June 2010)	"Contributions of Certain Nonfinancial Assets, Such as Fundraising Material, Informational Material, or Advertising, Including Media Time or Space for Public Service Announcements or Other Purposes"
TIS section 6140.23 (June 2010)	"Changing Net Asset Classifications Reported in a Prior Year"
TIS section 6930.02 (June 2010)	"Defined Benefit Plan Measurement of a Life Insurance Policy"
TIS section 5250.15 (June 2010)	"Application of Certain FASB Interpretation No. 48 (codified in FASB ASC 740-10) Disclosure Requirements to Nonpublic Entities That Do Not Have Uncertain Tax Positions"
TIS section 5250.14 (June 2010)	"Application of Financial Accounting Standards Board (FASB) Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (codified in FASB *Accounting Standards Codification* [ASC] 740-10) to Taxes Other Than Income Taxes "
TIS section 2240.06 (June 2010)	"Measurement of Cash Value Life Insurance Policy"
TIS section 2130.40 (June 2010)	"Certificates of Deposit and FASB ASC 320, *Investments—Debt and Equity Securities*"

(continued)

Recently Issued Technical Questions and Answers (AICPA, *Technical Practice Aids*)	
Accounting—continued	
TIS section 2130.39 (June 2010)	"Balance Sheet Classification of Certificates of Deposit"
TIS section 2130.38 (June 2010)	"Certificates of Deposit and Financial Accounting Standards Board (FASB) *Accounting Standards Codification* (ASC) 820, *Fair Value Measurements and Disclosures*"
TIS section 1800.05 (June 2010)	"Applicability of Fair Value Disclosure Requirements and Measurement Principles in Financial Accounting Standards Board (FASB) *Accounting Standards Codification* (ASC) 820, *Fair Value Measurements and Disclosures*, to Certain Financial Instruments "
TIS section 6910.33 (December 2009)	"Certain Financial Reporting, Disclosure, Regulatory, and Tax Considerations When Preparing Financial Statements of Investment Companies Involved in a Business Combination"
TIS section 2220.27 (December 2009)	"Determining Fair Value of Investments When the Practical Expedient Is Not Used or Is Not Available"
TIS section 2220.26 (December 2009)	"Categorization of Investments for Disclosure Purposes"
TIS section 2220.25 (December 2009)	"Impact of 'Near Term' on Classification Within Fair Value Hierarchy"
TIS section 2220.24 (December 2009)	"Disclosures—Ability to Redeem Versus Actual Redemption Request"
TIS section 2220.23 (December 2009)	"Adjusting NAV When It Is Not Calculated Consistent With FASB ASC 946"
TIS section 2220.22 (December 2009)	"Adjusting NAV When It Is Not as of the Reporting Entity's Measurement Date"
TIS section 2220.21 (December 2009)	"Determining Whether an Adjustment to NAV Is Necessary"
TIS section 2220.20 (December 2009)	"Determining Whether NAV Is Calculated Consistent With FASB ASC 946, *Financial Services—Investment Companies*"
TIS section 2220.19 (December 2009)	"Unit of Account"
TIS section 2220.18 (December 2009)	"Applicability of Practical Expedient"

Recently Issued Technical Questions and Answers (AICPA, *Technical Practice Aids*)	
Accounting—continued	
TIS section 6910.32 (July 2009)	"Additional Financial Statement Disclosures for Nonregistered Investment Partnerships When the Partnership Has Provided Guarantees Related to the Investee Fund's Debt"
TIS section 6910.31 (July 2009)	"The Nonregistered Investment Partnership's Method for Calculating Its Proportional Share of Any Investments Owned by an Investee Fund in Applying the '5 Percent Test' Described in TIS Section 6910.30"
TIS section 6910.30 (July 2009)	"Disclosure Requirements of Investments for Nonregistered Investment Partnerships When Their Interest in an Investee Fund Constitutes Less Than 5 Percent of the Nonregistered Investment Partnership's Net Assets"
TIS section 1600.04 (June 2009)	"Presentation of Assets at Current Values and Liabilities at Current Amounts in Personal Financial Statements"
TIS section 1500.07 (June 2009)	"Disclosure Concerning Subsequent Events in OCBOA Financial Statements"
Audit and Attest	
TIS section 1400.33 (July 2010)	"Combining Financial Statements Prepared in Accordance With the Income Tax Basis of Accounting"
TIS section 1800.06 (July 2010)	"Applicability of Fair Value Disclosure Requirements in Financial Accounting Standards Board (FASB) *Accounting Standards Codification* (ASC) 820, *Fair Value Measurements and Disclosures*, to Financial Statements Prepared in Conformity With a Comprehensive Basis of Accounting Other Than Generally Accepted Accounting Principles"
TIS section 8700.03 (June 2010)	"Auditor's Responsibilities for Subsequent Events Relative to a Conduit Debt Obligor"
TIS section 9110.16 (February 2010)	"Example Reports on Federal Deposit Insurance Corporation Loss Sharing Purchase and Assumption Transactions"
TIS section 8700.02 (September 2009)	"Auditor Responsibilities for Subsequent Events"
TIS section 8700.01 (September 2009)	"Effect of FASB ASC 855 on Accounting Guidance in AU Section 560"

Recent AICPA Independence and Ethics Developments

.189 The Audit Risk Alert *Independence and Ethics Developments—2010/11* (product no. 0224710) contains a complete update on new independence and ethics pronouncements. This alert will heighten your awareness of independence and ethics matters likely to affect your practice. Obtain this alert by calling the AICPA at (888) 777-7077 or visiting www.cpa2biz.com.

Establishing and Maintaining Internal Control

.190 One of the Professional Ethics Executive Committee's (PEEC's) current projects deals with a possible inconsistency within Interpretation No. 101-3, "Performance of Nonattest Services," under Rule 101, *Independence* (AICPA, *Professional Standards*, vol. 2, ET sec. 101 par. .05). Interpretation No. 101-3 provides examples of general activities that would impair a member's independence, including establishing or maintaining internal controls, including performing ongoing monitoring activities for a client. The PEEC recognizes that some practitioners perceive an inconsistency in Interpretation No. 101-3 because certain bookkeeping services and other nonattest services that are permitted under Interpretation No. 101-3 could be viewed as "maintaining internal control" for the client.

.191 To address the possible inconsistency in Interpretation No. 101-3, the PEEC is considering possible clarifying revisions to Interpretation No. 101-3. The revisions would provide more descriptive language about management responsibilities, which should help members better distinguish between permissible and prohibited nonattest services. Readers are encouraged to monitor the progress of this project.

.192 PEEC meeting information, including meeting agendas, discussion materials, and minutes of prior meetings can be found at www.aicpa.org/InterestAreas/ProfessionalEthics/Community/MeetingMinutesandAgendas/Pages/MeetingInfo.aspx.

.193 Exposure drafts issued by the PEEC can be found at www.aicpa.org/InterestAreas/ProfessionalEthics/Community/ExposureDrafts/Pages/ExposureDrafts.aspx.

On the Horizon

.194 Auditors should keep abreast of auditing and accounting developments and upcoming guidance that may affect their engagements. The following sections present brief information about some ongoing projects that have particular significance to the health care industry or that may result in significant changes. Remember that exposure drafts are nonauthoritative and cannot be used as a basis for changing existing standards.

.195 Information on, and copies of, outstanding exposure drafts may be obtained from the various standard setters' websites. These websites contain in-depth information about proposed standards and other projects in the pipeline. Many more accounting and auditing projects exist in addition to those discussed here. Readers should refer to information provided by the various standard setting bodies for further information.

Overhaul Project—AICPA Audit and Accounting Guide *Health Care Entities*

.196 The AICPA is continuing to make progress overhauling the AICPA Audit and Accounting Guide *Health Care Entities*, addressing numerous accounting, auditing, industry, and regulatory issues that have transpired since this guide was originally issued in 1996. During this project, the AICPA will continue to issue annual editions of the guide, updated to reflect recent audit and accounting pronouncements.

Auditing and Attestation Pipeline—Nonissuers

ASB Clarity Project

.197 In response to growing concerns about the complexity of standards, the ASB has commenced a large-scale clarity project to revise all existing auditing standards so they are easier to read and understand. Over the last few years, the ASB has been redrafting all of the existing auditing sections contained in the *Codification of Statements on Auditing Standards* (AU sections of the AICPA's *Professional Standards*) to apply the clarity drafting conventions and converge with the ISAs issued by the IAASB. The majority of the clarified standards will be issued in a single SAS codified as AU sections, with each section assigned a section number and title. When the new SAS becomes effective, the SASs issued prior to SAS No. 117, *Compliance Audits* (AICPA, *Professional Standards*, vol. 1, AU sec. 801), will be superseded. The ASB proposes that most redrafted standards become effective at the same time and is working toward completing the project in the first half of 2011. Two possible exceptions to that timeframe include the clarity redrafts of AU section 341, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern,* and AU section 532, *Restricting the Use of an Auditor's Report* (AICPA, *Professional Standards*, vol. 1).

.198 In May 2010, the expected effective date of the clarified standards was revised to be applicable for audits of financial statements for periods ending on or after December 15, 2012. The standards recently issued in clarified format (SAS Nos. 117–120) have different effective dates. The ASB believes that having a single effective date for most of the clarified standards will ease the transition to, and implementation of, the redrafted standards. The effective date will be long enough after all redrafted statements are finalized to allow sufficient time for training and updating of firm audit methodologies. This expected date depends on satisfactory progress being made and will be amended, if necessary. Further, early adoption of the new SAS will not be appropriate. The SAS that will encompass all clarified AU sections will be issued with the next consecutive number that is available. See the explanatory memorandum "Clarification and Convergence," the discussion paper *Improving the Clarity of ASB Standards*, and *Clarity Project: Questions and Answers* at www.aicpa.org/InterestAreas/AccountingAndAuditing/Resources/AudAttest/AudAttestStndrds/ASBClarity/Pages/ImprovingClarityASBStandards.aspx. All clarified SASs that have been finalized by the ASB but are not yet issued as authoritative can be found at www.aicpa.org/InterestAreas/AccountingAndAuditing/Resources/AudAttest/AudAttestStndrds/ASBClarity/Pages/Final%20Clarified%20Statements%20on%20Auditing%20Standards.aspx.

Interim Financial Information

.199 In July 2010, the ASB issued two proposed SASs on interim financial information. The first, *Revised Applicability of Statement on Auditing Standards No. 116*, Interim Financial Information, is intended to revise paragraph 5 of SAS No. 116 (AICPA, *Professional Standards*, vol. 1, AU sec. 722), so that the guidance in SAS No. 116 would be applicable when the auditor audited the entity's latest annual financial statements and the appointment of another auditor to audit the current year financial statements is not effective prior to the beginning of the period covered by the review. Currently, the guidance in SAS No. 116 is applicable when the auditor performs the audit of the latest annual financial statements and expects to be engaged to audit the current year financial statements (and, therefore, is not applicable when the auditor expects that a new auditor may be engaged for the current year). This proposed amendment would be effective for interim reviews of interim financial information for periods beginning after December 15, 2011, with early implementation permitted. Comments are due by October 8, 2010.

.200 The second proposal on interim financial information, *Interim Financial Information* (Redrafted), would supersede SAS No. 116 and represents the redrafting of the guidance to apply clarity drafting conventions. The main changes to existing standards are as follows:

- Replacement of the term *accountant* with *auditor*
- The change to paragraph 5 discussed in the prior paragraph
- Requirement of the auditor to issue a written report unless the review of the interim financial information is required by a third party and the third party does not require a written review report
- Allowance of oral reports for entities that are subject to external requirements to report in a manner that is substantially similar to the reporting required of issuers, pursuant to PCAOB standards
- Requirement for the auditor to perform procedures consistent with those required for acceptance of an engagement to audit financial statements
- Requirement for the review report to include a statement that the review of interim financial information was conducted in accordance with auditing standards generally accepted in the United States of America

.201 This proposed SAS would be effective for reviews of interim financial information for interim periods of fiscal years beginning on or after December 15, 2012. Comments for this proposed SAS are also due by October 8, 2010.

Exposure Drafts on Auditor's Reports

.202 The ASB issued three proposed SASs related to auditor's reports: *Forming an Opinion and Reporting on Financial Statements*, *Modifications to the Opinion in the Independent Auditor's Report*, and *Emphasis of Matter Paragraphs and Other Matter Paragraphs in the Independent Auditor's Report*. These proposed standards are drafted with the ASB's clarity drafting conventions and are intended to converge with ISAs. The intent of issuing three separate SASs is to assist practitioners in identifying and applying the reporting requirements and guidance. The ASB has made various changes to the related

ISAs to tailor them to the United States; however these changes have not been substantial in nature.

.203 The proposed SASs are expected to be effective for audits of financial statements for periods ending on or after December 15, 2012. Auditors are encouraged to review the exposure draft and be alert for developments on this topic.

Exposure Drafts on Special Considerations Audits

.204 Another exposure draft issued by the ASB contains two proposed SASs: *Special Considerations—Audits of Financial Statements Prepared in Accordance With Special Purpose Frameworks and Special Considerations—Audits of Single Financial Statements* and *Specific Elements, Accounts, or Items of a Financial Statement*. These proposed standards have been drafted with the clarity drafting conventions and are intended to converge with the equivalent ISAs. No meaningful differences exist between these proposed standards and the ISAs. *Special Considerations—Audits of Financial Statements Prepared in Accordance With Special Purpose Frameworks* addresses the application of GAAS to financial statements prepared under the cash, tax, regulatory, or contractual bases of accounting. It also replaces the term other comprehensive basis of accounting with special purpose framework.

.205 *Special Considerations—Audits of Single Financial Statements and Specific Elements, Accounts, or Items of a Financial Statement* introduces new planning, performance, and reporting requirements for these engagements. The proposed SAS also clarifies that a single financial statement and a specific element of a financial statement include the related notes.

.206 The comment period for the proposed SASs ended in December 2009. The proposed SASs are expected to be effective for audits of financial statements for periods ending on or after December 15, 2012. Auditors are encouraged to review the exposure draft and be alert for developments on this topic.

Auditing and Attestation Pipeline—Issuers

Confirmations

.207 The PCAOB has proposed a draft of an auditing standard on confirmations. A concept release was originally issued in April 2009 and received 24 comment letters. This proposed auditing standard, issued in July 2010, would strengthen the requirements under the current auditing standard, AU-P section 330, *The Confirmation Process* (AICPA, *PCAOB Standards and Related Rules*, Standards), and replace it, upon final issuance of a standard and approval from the SEC. The proposed new standard

- requires confirmation procedures for specific accounts, such as receivables that arise from credit sales, loans, or other transactions, and also in response to significant risks that relate to the relevant assertions that can be adequately addressed by confirmation procedures.
- incorporates procedures in response to the risk of material misstatement, such as in the areas of investigating exceptions reflected on confirmation responses and evaluating nonresponses to confirmation requests.

- updates the confirmation guidance to reflect significant advances in technology and explains that confirmation responses received electronically (for example, by fax e-mail, through an intermediary, or direct access) might involve additional risks relating to reliability. Therefore, the auditor must perform additional requirements.
- defines a confirmation response to include electronic or other medium.
- enhances requirements when confirmation responses include disclaimers and restrictive language by requiring the auditor to evaluate the effect on the reliability of a confirmation response. Further, if the disclaimer or restrictive language causes doubts about the reliability of a confirmation response, the auditor should obtain additional appropriate audit evidence.

.208 In drafting this proposed standard, the PCAOB considered the guidance contained in ISA 505, *External Confirmations*, and the AICPA's proposed guidance on confirmations. This standard is anticipated to be effective for auditors for fiscal years ending on or after December 15, 2011.

Communications With Audit Committees

.209 In March 2010, the PCAOB proposed for comment an auditing standard on *Communications with Audit Committees* and a series of related amendments to its interim standards that are intended to (*a*) enhance the relevance and effectiveness of the communications between the auditor and the audit committee and (*b*) emphasize the importance of effective, two-way communications between the auditor and the audit committee to better achieve the objectives of the audit. Two of the new requirements would be for the auditor (*a*) to establish a mutual understanding of the terms of the audit engagement with the audit committee and to document that understanding in the engagement letter and (*b*) to evaluate the adequacy of two-way communication between the auditor and audit committee. Additionally, the proposal also includes requirements for the auditor to communicate with the audit committee regarding the following:

- An overview of the audit strategy and timing of the audit, including a discussion of significant risks; the use of the internal audit function; and the roles, responsibilities, and location of firms participating in the audit
- Critical accounting policies, practices, and estimates
- The auditor's evaluation of the entity's ability to continue as a going concern

.210 The proposed standard would become effective, subject to SEC approval, for audits of fiscal years beginning after December 15, 2010.

Joint FASB and IASB Accounting Pipeline

FASB and IASB Memorandum of Understanding

.211 The year 2010 has been a pivotal year of progress toward the goal of completing the important projects in the "Memorandum of Understanding" (MoU) during 2011. Since its original issuance in 2006, FASB and the IASB have continued to reaffirm their respective commitments to the development of high quality, compatible accounting standards that could be used for both domestic and cross-border financial reporting. FASB and the IASB agreed that the goal of joint projects is to produce common, principles-based standards, subject to the required due process. FASB and the IASB have agreed to intensify their efforts to complete the major joint projects described in the MoU and are committed to developing, and making publicly available, quarterly progress reports on these major projects. The MoU identifies 11 convergence topics:

- Financial instruments
- Consolidations
- Derecognition
- Fair value measurement
- Revenue recognition
- Leases
- Financial instruments with characteristics of equity
- Financial statement presentation
- Balance sheet netting
- Statement of comprehensive income
- Discontinued operations

.212 A progress report for the quarter ended March 31, 2010, highlighted the following topics: (*a*) on the financial instruments and insurance contracts topics, the boards have reached different conclusions on significant technical issues that may affect the project timetables of these topics and (*b*) the boards agreed to explore an alternative approach to lessor accounting that may affect the project timetable of this topic. FASB and the IASB also have several other joint projects in process, including balance sheet—offsetting, emissions trading schemes, and reporting discontinued operations. In March 2010, the exposure draft *Conceptual Framework for Financial Reporting* was published for public comment. In early June 2010, the boards issued a joint statement that discusses the boards' recognition of the challenges that arise from seeking effective global stakeholder feedback. Specifically, the boards were scheduled to expose for comment numerous major exposure drafts during the second quarter of 2010, and stakeholders voiced concern about their ability under those circumstances to provide high-quality input. The boards have developed a modified strategy to accommodate these concerns by prioritizing the major projects in the MoU, staggering the publication of exposure drafts by limiting the number of significant exposure drafts to four per quarter, and issuing a separate consultation document seeking stakeholder input about effective dates and transition methods.

.213 The priority joint projects are financial instruments, revenue recognition, leases, the presentation of other comprehensive income, and fair value measurements. The boards also decided to issue separate exposure drafts to address differences in the two sets of standards on balance sheet netting of derivative contracts and other financial instruments. The IASB has also made its projects on improved disclosures about derecognized assets and other off balance sheet risks, consolidations, and insurance contracts priorities. June 2011 or earlier will remain the target completion date for these priority convergence projects; the target completion dates for the nonpriority projects, however, have been extended into the second half of 2011. Additionally, the comments received on exposure drafts will affect the timeline of finalized converged standards. The boards' joint statement states that this action is not expected to negatively affect the SEC's work plan to consider in 2011 whether and how to incorporate IFRSs into the U.S. financial system.

.214 Readers are encouraged to remain current for the remainder of the exposure draft releases and other developments on convergence through the AICPA's website, www.ifrs.com, in addition to the FASB, IASB, and SEC websites. The growing acceptance of IFRSs as a basis for U.S. financial reporting could represent a fundamental change for the U.S. accounting profession.

Comprehensive Income Exposure Draft

.215 In May 2010, FASB issued a proposed ASU on comprehensive income that would require an entity to report total comprehensive income in a continuous financial statement in two parts: net income and other comprehensive income. In that financial statement, the components of net income and the components of other comprehensive income should be displayed. The proposed ASU is intended to simplify how comprehensive income is reported by eliminating two options for how items of comprehensive income are displayed. The proposed ASU contains illustrative examples of the revised financial statement. This proposed ASU is the result of a joint project as part of IFRSs and U.S. GAAP convergence, and the IASB has separately issued a similar document. The proposed amendments would be applied on a fully retrospective basis to improve comparability between reporting periods. Further, because compliance with the proposed amendments is already permitted, early adoption would be permitted. FASB plans to align the effective date with the effective date of the amendments in the proposed ASU on financial instruments. The IASB and FASB aim to finalize an improved and converged standard on other comprehensive income in the fourth quarter of 2010.

Financial Instruments Exposure Draft

.216 Also, in May 2010, FASB issued a proposed ASU on accounting for financial instruments, derivative instruments, and hedging activities. The main objective of this proposal is to provide financial statement users with a more timely and representative depiction of an entity's involvement in financial instruments while reducing the complexity in accounting for those instruments. It develops a consistent framework for classifying financial instruments, removes the threshold for recognizing credit impairments, creating a single credit impairment model for both loans and debt securities; and makes changes to the requirements to qualify for hedge accounting. The main provisions of these amendments are as follows:

- Most financial instruments would be measured at fair value in the statement of financial position each reporting period.
- Changes in fair value of equity securities, certain hybrid instruments, and financial instruments that can be prepaid in such a way that the holder would not recover substantially all of its investment would be recognized in net income each reporting period regardless of an entity's business strategy for those financial instruments.
- Hybrid financial instruments containing embedded derivatives that would otherwise have been required to be bifurcated under FASB ASC 815-15 would be classified and measured at fair value in their entirety, with changes accounted for through net income.

- For financial instruments for which an entity's business strategy is to hold for collection or payment(s) of contractual cash flows, a reconciliation from amortized cost to fair value would be required on the statement of position; with the exception of certain liabilities that qualify for the amortized cost option, all other changes in fair value from these instruments would be recognized in other comprehensive income each reporting period. Therefore, net income will remain relatively unchanged because only changes arising from interest accruals, credit impairments, and realized gains and losses would be recognized in net income each reporting period.
- The existing probable threshold for recognizing impairments on loans would be removed. (Currently, FASB ASC 310-10-35-4 states that the concept in U.S. GAAP is that impairment of receivables [including loans] should be recognized when, based on all available information, it is probable that a loss has been incurred based on past events and conditions existing at the date of the financial statements. Probable is defined by FASB ASC 310-10-20 as when the future event or events are likely to occur.)
- For changes in the value of financial instruments measured through other comprehensive income, an entity is required to determine if a credit impairment is appropriate at the end of each reporting period based on information related to past events and existing economic conditions. An entity would recognize in net income the loss related to the amount of credit impairment for all contractual amounts the entity does not expect to collect.
- Core deposit liabilities would be remeasured each period using a current value method that reflects the economic benefit that an entity receives from this lower cost, stable funding source.
- Interest income would be recognized after considering cash flows that are not expected to be collected, which would better reflect a financial instrument's interest yield.
- Quantitative-based hedging requirements would be replaced with more qualitative-based assessments that would make it easier to qualify for hedge accounting. The shortcut method and critical terms match method would be eliminated. An entity would be able to designate particular risks as the risk being hedged in a hedging relationship, and only the effects of the risks hedged would be reflected in net income.
- Hedge accounting would be discontinued only if the criteria for hedge accounting are no longer met or the hedging instrument expires or is sold, terminated, or exercised. An entity would not be permitted to discontinue hedge accounting by simply removing the designation of a hedging relationship.

.217 Some specific types of financial instruments, such as pension obligations and leases, would be exempt from the proposed guidance. Additionally, short term receivables and payables would continue to be measured at amortized cost (plus or minus any fair value hedging adjustments). This proposed ASU was not issued jointly with the IASB and does not contain converged guidance; however, the goal still remains for both boards to issue comprehensive improvements to foster international comparability of financial information about financial instruments. The IASB completed its first phase of classification and measurement with the issuance of IFRS 9, *Financial Instruments*, in November 2009. The IASB also issued two exposure drafts on amortized cost and impairment and fair value option for financial liabilities in late 2009 and mid-2010, respectively; the third topic, hedge accounting, is still being deliberated by the IASB, and an exposure draft is expected in the near term. The boards have stated that they will consider together the comment letters and other feedback received on each boards' exposure drafts in an effort to reconcile their differences in ways that foster improvement and convergence.

.218 The effective date of these amendments will be established upon issuance of the final ASU, which is expected in the second quarter of 2011; it is estimated to have an effective date in 2013. However, nonpublic entities with less than $1 billion in total consolidated assets would be granted an additional 4 years to implement certain requirements related to loans and core deposits. Upon its application, an entity would apply the proposed guidance by means of a cumulative-effect adjustment to the statement of financial position for the reporting period that immediately precedes the effective date.

.219 FASB has issued frequently asked questions for the proposed ASU to clarify the proposal by answering common questions received about the proposed guidance. This document can be accessed at www.fasb.org/cs/ContentServer?c=Document_C&pagename=FASB%2FDocument_C%2FDocumentPage&cid=1176157295447.

Revenue Recognition Exposure Draft

.220 The revenue recognition project is intended to develop a single, common revenue recognition model that can be applied to a wide range of industries and transaction types. The standards resulting from this project will eliminate weaknesses and inconsistencies between the existing standards. A joint discussion paper issued by the boards proposed a single revenue recognition model. A joint exposure draft, *Revenue from Contracts with Customers*, from the boards was published in June 2010, and the boards aim to issue a final converged standard by the second quarter of 2011. The proposed standard would replace International Accounting Standard (IAS) 18, *Revenue*; IAS 11, *Construction Contracts*; and related interpretations in IFRSs; under U.S. GAAP, it would supersede most of the guidance contained in FASB ASC 605, *Revenue Recognition*. The core principle of the draft standard is that an entity should recognize revenue from contracts when it transfers goods or services to the customer in the amount of consideration the entity receives, or expects to receive, from the customer.

.221 In addition to eliminating weaknesses and inconsistencies between IFRSs and U.S. GAAP, this proposal intends to provide a more robust framework for addressing various revenue recognition issues; improve comparability of revenue recognition practices across entities, industries, jurisdictions, and capital markets; and simplify the preparation of financial statements by reducing the number of requirements to which entities must refer. The proposed standard will also amend the existing guidance on recognition of a gain or loss on the sale of some nonfinancial assets that are not an output of the entity's ordinary activities (for example, property, plant, and equipment) to be consistent with the proposed revenue recognition and measurement requirements. To implement the preceding core principle of revenue recognition, an entity would

- identify the contract(s) with the customer.
- identify the separate performance obligations in the contract (performance obligation is an enforceable promise [whether explicit or implicit] in a contract with a customer to transfer a good or service to the customer).
- determine the transaction price (transaction price is the amount of consideration that an entity receives, or expects to receive, from a customer in exchange for transferring goods or services promised in the contract).
- allocate the transaction price to the separate performance obligations.
- recognize revenue when the entity satisfies each performance obligation by transferring a promised good or service to a customer (a good or service is transferred when the customer obtains control of that good or service).

.222 The proposal also includes guidance on accounting for some costs. An entity would recognize the costs of obtaining a contract as expenses when incurred. For expenses incurred in fulfilling a contract, if they are ineligible for capitalization in accordance with other guidance, an entity would only be able to recognize an asset if those costs relate directly to a contract (or a specific contract under negotiation); generate or enhance resources of the entity that will be used in satisfying performance obligations in the future; and are expected to be recovered. The proposed guidance would differ from current practice in the following ways: (*a*) recognition of revenue only from the transfer of goods or services, (*b*) identification of separate performance obligations, (*c*) licensing and rights to use, (*d*) effect of credit risk, (*e*) use of estimates, (*f*) accounting for costs, and (*g*) disclosure.

.223 As discussed previously, because the revenue recognition project is one of many standards the boards expect to issue as converged and final in 2011, the boards plan to invite additional comment through a separate consultation on how best to transition over to the new standards. Therefore, no expected specific effective date is stated at this point. Comments on the exposure draft are due on October 22, 2010. This topic is considered by many to be the most pervasive of any FASB has ever worked on. The reader is encouraged to review the exposure draft, consider if it is operational to you or your clients' common revenue transactions, and share any resulting concerns with FASB. The boards also anticipate holding public roundtable meetings after the end of the comment period.

Fair Value Exposure Draft

.224 The fourth and final exposure draft of the second quarter of 2010 was *Fair Value Measurements and Disclosures (Topic 820): Amendments for Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs*. The amendments in the exposure draft are intended to result in common fair value measurement and disclosure requirements in financial statements prepared in accordance with U.S. GAAP and IFRSs. Many of the requirements are not intended to result in a change in the application of the requirements in FASB ASC 820; however, some are intended to clarify or change the application of existing fair value guidance. Additionally, some wording changes were made to ensure the guidance is described consistently between U.S. GAAP and IFRSs. The most significant proposed amendments include the following:

- Highest and best use and valuation premise
- Measuring the fair value of an instrument classified in shareholders' equity
- Measuring the fair value of financial instruments that are managed within a portfolio
- Application of blockage factors and other premiums and discounts in a fair value measurement
- Additional disclosures about fair value measurements

.225 The first two of these significant amendments are intended to clarify the application of existing fair value measurement guidance. The last three of these significant amendments would change a particular principle of fair value guidance.

.226 The amendments would specify that the concepts of highest and best use and valuation premise in a fair value measurement are relevant only when measuring the fair value of nonfinancial assets, not when measuring the fair value of financial assets or liabilities. The FASB ASC glossary defines *highest and best use* as, in broad terms, the use of an asset by market participants that would maximize the value of the asset or the group of assets within which the asset would be used. The rationale for this proposed change is that the highest and best use concept is irrelevant when measuring the fair value of financial assets or liabilities because these items do not have alternative uses and their fair values do not depend on their use within a group of other assets or liabilities. These changes are not expected to affect the fair value measurement of nonfinancial assets. However, they might affect current practice for reporting entities that apply the in-use valuation premise more broadly.

.227 The amendments related to measuring the fair value of an instrument classified in shareholders' equity would specify that a reporting entity should measure the fair value of its own equity instrument from the perspective of a market participant who holds the instrument as an asset. An example of an instrument that would be measured at fair value and classified in shareholders' equity is equity interests issued as consideration in a business combination. Currently, U.S. GAAP does not contain explicit guidance on this topic, and the proposed amendments are expected to increase the comparability among reporting entities applying U.S. GAAP and IFRSs.

.228 Regarding measuring the fair value of financial instruments that are managed within a portfolio, the proposed amendments would allow an exception to FASB ASC 820 for measuring fair value when a reporting entity manages its net exposure, rather than its gross exposure, to the underlying risks. A reporting entity that holds a group of financial assets and financial liabilities is exposed to interest rate risk, currency risk, or other price risk (market risks) and to the credit risk of each of the counterparties. The proposed guidance is intended to coincide with financial institutions and other similar reporting entities that hold and manage these instruments in that manner. Specifically, a reporting entity could measure the fair value of the financial assets and financial liabilities that are managed in that way on the basis of the price that would be received to sell a net long position (that is, an asset) for a particular risk or to transfer a net short position (that is, a liability) for a particular risk in an orderly transaction between market participants at the measurement date. The proposed amendments would result in U.S. GAAP and IFRSs having the same requirements for measuring the fair value of financial instruments; additionally, these changes would not change how financial assets and financial liabilities that are managed on the basis of a reporting entity's net risk exposure are measured in practice. However, they might affect the current practice for reporting entities that apply the in-use valuation premise more broadly.

.229 The proposed amendments regarding the application of blockage factors and other premiums and discounts in fair value measurements would make two changes to current guidance. Currently, under U.S. GAAP, use of a blockage factor in fair value measurements is only prohibited when fair value is measured using a quoted price for an asset or a liability (or similar assets or liabilities). This would be level 1 within the fair value hierarchy. The first change from the proposed amendments is that a blockage factor is not relevant and, therefore, also should not be used when fair value is measured using a valuation technique that does not use a quoted price. This would be level 2 or level 3 within the fair value hierarchy. Second, the amendments specify that fair value measurements categorized within level 2 and level 3 take into account other premiums and discounts when market participants would consider those premiums or discounts when pricing an asset or a liability, consistent with the unit of account for that asset or liability. Examples include a control premium or a noncontrolling interest discount. These proposed amendments may affect current practice for any reporting entities applying a blockage factor in fair value measurements that is measured using quoted prices and categorized within level 2 of the fair value hierarchy.

.230 Lastly, the amendments propose additional disclosures about fair value measurements. More information about the following would be required for disclosure:

- The effect on a fair value measurement of changing one or more unobservable inputs that could have reasonably been used to measure fair value in the circumstances
- Use of an asset in a way that differs from the asset's highest and best use when that asset is recognized at fair value in the statement of financial position on the basis of its highest and best use
- The categorization by level within the fair value hierarchy for items that are not measured at fair value in the statement of financial position but for which the fair value of such items is required to be disclosed

.231 The effective dates of these proposed amendments would be determined after the feedback from the exposure draft is considered. However, when it is effective, it will be effective as of the beginning of the period of adoption, and an entity would recognize a cumulative effect adjustment in beginning retained earnings in the period of adoption if a difference exists in a fair value measurement of an item recorded at fair value as a result of applying these amendments. Additional disclosures would be required on a prospective basis. These amendments are expected to achieve the objective of developing common fair value measurement and disclosure requirements in U.S. GAAP and IFRSs. A final ASU is expected to be issued in the first quarter of 2011.

Financial Statement Presentation Staff Draft

.232 FASB and the IASB are working together to establish a common standard that would improve how information is organized and presented in

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financial statements. This common standard is intended to address users' concerns that existing requirements permit too many alternative types of presentation and that information in financial statements is highly aggregated and inconsistently presented, making it difficult to fully understand the relationship between an entity's financial statements and its financial results. In 2008, a discussion paper was issued by the boards that outlined the proposed principles for presenting financial statements in a way that portrays a cohesive financial picture of an entity.

.233 Given the magnitude of this project, the expected implementation costs, and the substantial effects it will have on financial statement presentation for many years to come, the boards decided in May 2010 to modify the strategy for this project. Before finalizing an exposure draft, the boards decided to engage in additional outreach activities that focus on the perceived benefits and costs of the proposals and the implications of the proposals for financial reporting by financial service entities. The boards plan on discussing these two areas of focus with preparers and users of financial statements. This outreach will be based on a rough draft of a proposed standard, known as a *staff draft*, and reflects the cumulative tentative decisions made by the boards, concluding with their joint meeting in April 2010. This staff draft was made publicly available solely for this purpose.

.234 The proposals in this project would be applicable to all entities, except a benefit plan within the scope of FASB ASC 960, *Plan Accounting—Defined Benefit Pension Plans*; FASB ASC 962, *Plan Accounting—Defined Contribution Pension Plans*; and FASB ASC 965, *Plan Accounting—Health and Welfare Benefit Plans*, or IAS 26, *Accounting and Reporting by Retirement Benefit Plans*. The two core financial statement principles in this proposal are cohesiveness and disaggregation. A common structure for the statements of financial position, comprehensive income, and cash flows would be established in the form of required sections, categories or subcategory, and related subtotals. Some proposed specific changes in the classification and format of financial statements include the following:

- Related information would be displayed in the same sections, categories, and subcategory in each statement so that information is more easily associated.
- Presentation of business and financing activities would be separated as follows:
  - — The business section would include items that are part of an entity's daily operations and other income generating activities.
  - — The financing section would include items that are part of an entity's activities to obtain (or repay) capital.
- Discontinued operations and income taxes would be presented in their own separate sections.
- The statement of changes in equity would not include the sections and categories used in the other statements because that statement presents information solely about changes in items classified in the equity category in the statement of financial position.

.235 Further, FASB plans to propose some changes that are already required by IAS 1, *Presentation of Financial Statements*. The proposal would

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define and provide the requirements for a complete set of financial statements. Currently, a complete set of financial statements for the period is defined only in the FASB Concepts Statements. An entity would also be required to present one period of comparative information. A complete set of financial statements would consist of, at a minimum, statements of financial position, comprehensive income, cash flows and changes in equity, and notes to financial statements for two periods (the current period and the previous period). Also, an opening statement of financial position would be part of a complete set of financial statements if an entity applies an accounting principle retrospectively, restates its financial statements, or reclassifies items in the financial statements.

.236 The boards' tentative decisions on financial statement presentations do differ in a few ways in relation to minimum line requirements for the statement of financial position, segment reporting, and net debt presentation. Of these three, the differing stance on segment reporting is the only significant difference. The boards now aim to issue an exposure draft in the first quarter of 2011 and a final improved and converged standard in the fourth quarter of 2011. Both the introduction to the staff draft and the staff draft can be accessed from FASB's website at www.fasb.org.

Leases Exposure Draft

.237 During the third quarter of 2010, the IASB and FASB published for public comment joint proposals to improve the financial reporting of lease contracts. These proposals would result in a consistent approach to lease accounting for both lessees and lessors—a "right of use" approach. This would result in the liability for payments arising under the lease contract and the right to use the underlying asset being included in the lessee's statement of financial position, therefore providing more complete and useful information to investors and other users of financial statements. Currently, the accounting for a lease depends on its classification; an operating lease results in the lessee not recording any assets or liabilities in the statement of financial position under either IFRSs or U.S. GAAP, whereas a capital lease results in the lessee recognizing an asset and an obligation. Under the proposed guidance, lessees would only have one method of accounting for leases, which would produce more complete and comparable financial reporting in addition to reducing the opportunity to structure transactions to achieve a desired accounting outcome.

.238 The scope of the new lease guidance includes all leases (including leases of right-of-use assets in a sublease) other than leases of biological and intangible assets, leases to explore for or use natural resources, and leases of some investment properties. Under this new guidance, all lessees would use a single method of accounting for all leases: an asset would be recognized representing the lessee's right to use the leased (underlying) asset for the lease term (the right-of-use asset), and a liability at the present value of the expected lease payments would also be recognized.

.239 A lessor would recognize an asset representing its right to receive lease payments and, depending on its exposure to risks or benefits associated with the underlying asset, would either (*a*) recognize a lease liability while continuing to recognize the underlying asset (a *performance obligation approach*); or (*b*) derecognize the rights in the underlying asset that it transfers to the lessee and continue to recognize a residual asset representing its rights to the underlying asset at the end of the lease term (a *derecognition approach*). The

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assets and liabilities recognized by both lessors and lessees would be measured on the basis that

- assumes the longest possible lease term that is more likely than not to occur, taking into account the effect of any options to extend or terminate the lease.
- uses an expected outcome technique to reflect the lease payments, including contingent rentals and expected payments under term option penalties and residual value guarantees, specified by the lease.
- a remeasurement is triggered when changes in facts or circumstances indicate that there would be a significant change in those assets or liabilities since the previous reporting period.

.240 For leases of 12 months or less, lessors and lessees would be able to apply simplified requirements. The simplified accounting would allow lessees to ignore the effects of interest on the recorded assets and liabilities and allow the lessee to record the liability for lease payments at the undiscounted amount for lease payments. New disclosures would also be required.

.241 In early 2009, the boards issued a discussion paper on leases; this exposure draft is the result of extensive deliberations that included consideration of input received from investors, preparers, auditors, regulators, and other interested parties since that discussion paper. The comment period is open until December 15, 2010. During the comment period, the boards will undertake further outreach activities, including public round-table meetings to ensure that the views of all interested parties are taken into consideration before the new standard is completed. Also, the boards will share and jointly consider all comment letters received. A final standard is expected in the second quarter of 2011. The AICPA has developed questions and answers to highlight the important aspects of the proposals, which can be located at www.aicpa.org/InterestAreas/AccountingAndAuditing/Resources/AcctgFinRptg/AcctgFinRptgGuidance/DownloadableDocuments/EDITED_LEASES_FAQ.pdf.

Insurance Contracts Discussion Paper

.242 In June 2010, the IASB issued an exposure draft of a proposed IFRS that would apply to all insurance contracts written by both insurance entities and noninsurance entities. Three months later, FASB issued a discussion paper to solicit broad-based input on how to improve, simplify, and converge the financial reporting requirements for insurance contracts. The solicited feedback is focused on (*a*) whether the IASB's proposal would be a sufficient improvement to U.S. GAAP to justify the cost of change; (*b*) whether the project goals of improvement, convergence, and simplification would be more effectively achieved by making targeted improvements to existing U.S. GAAP (rather than issuing comprehensive new guidance); and (*c*) certain critical accounting issues for which the preliminary views of FASB differ from the IASB's exposure draft. It is important to remember that although the project on insurance contracts is a joint project, it is not part of the boards' MoU.

.243 The discussion paper summarizes the key aspects of the IASB's exposure draft and compares the proposed changes with both the alternative preliminary views of FASB and the current guidance in FASB ASC 944, *Financial Services—Insurance*. FASB decided to issue a discussion paper rather than an exposure draft because of the following reasons:

- The extent of FASB's and the IASB's current accounting guidance for insurance contracts varies significantly; U.S. GAAP comprehensively addresses accounting for insurance contracts by insurance entities, whereas IFRSs do not have comprehensive guidance. Further, the boards have not explicitly evaluated whether the model proposed in the IASB's exposure draft would represent an improvement to U.S. GAAP.
- FASB has not determined whether one model or two models would result in more useful information about insurance contracts. FASB would like additional input from stakeholders on whether different types of insurance contracts warrant different recognition, measurement, and presentation and, if so, what criteria should be used for determining which, if any, types of insurance contracts would use each model.
- FASB is considering whether employer-provided health insurance should be included within the scope of the insurance contracts project and how recent U.S. health care reform may affect the application of the different approaches.

.244 The discussion paper also includes a listing of common elements of U.S. GAAP on insurance contracts that some stakeholders note could be improved. The appendix of the discussion paper compares the main areas of current U.S. GAAP for insurance contracts, the IASB's proposed approach, and FASB's preliminary views that differ from the proposed approach included in the IASB's exposure draft. Comments are due by mid-December 2010. Additionally, FASB and the IASB plan to host a series of public roundtable meetings in December 2010 to hear stakeholders' views. Readers should be alert for developments on this topic.

Auditing Considerations of Accounting Convergence

.245 Although the future of convergence between IASB and FASB accounting standards remains an unknown, discussions have already begun about the potential impact on auditors. Although auditors are accustomed to new standards, the nature and volume of these changes will likely pose new challenges. Among others, some of these potential challenges include the following:

- Training audit staff on a large amount of new accounting guidance that is based on an accounting approach (that is, principles based versus rules based)
- Developing, as necessary, any new internal audit guidance, such as firm methodology
- Implementing any new resulting auditing rules
- Creating a new framework for documenting audit conclusions on a principles-based accounting approach
- Audit committees learning new accounting guidance to effectively perform their function

.246 In addition to the challenges auditors will face, the effects on preparers will also be great. At the time of this writing, it appears that the transition timeline to convergence will be relatively short; this will divert resources during the preparation of financial statements as entities focus on implementing the new principles, which may result in increased audit risk. Auditors, in addition to preparers, are also encouraged to remain current on developments of international accounting convergence.

FASB Accounting Pipeline

Health Care Entities: Revenue Recognition Exposure Draft

.247 FASB has a project on revenue recognition for health care entities. The issue is whether collectability must be reasonably assured prior to a health care entity recognizing revenue. Health care entities may perform services for which the ultimate collection of all or a certain portion of the amount billed or billable is not expected in its entirety, is doubtful, or cannot be determined at the time the services are rendered. In some situations (for example, charity care), health care entities record no revenue. For billings to self-pay patients, it has been industry practice for health care entities to adopt a revenue recognition policy to record revenue at the gross charge along with a relatively high bad debt provision, as provided for in FASB ASC 904-605-25-3. Health care entities that apply this policy also record revenue for insured patients when services are provided and adjust that revenue for contractual allowances (discounts) based on third-party payor or other arrangements. A bad debt provision is typically recorded for the amount due for deductibles and copays judged to be uncollectible. The bad debt provision is generally classified as an expense and not as a reduction to revenue.

.248 The effective date for the proposed amendments would be determined after the exposure period. Readers should be alert to the development of this topic.

Fees Paid to the Federal Government by Pharmaceutical Manufacturers *Exposure Draft*

.249 In August 2010, FASB issued a proposed ASU on accounting for certain fees associated with recently enacted health care legislation. The issues are (*a*) how the annual fee imposed by the PPACA and the Health Care and Education Reconciliation Act of 2010 (HCERA) should be classified in a reporting entity's income statement and (*b*) whether the annual fee should be expensed in its entirety when the liability is recognized or whether an asset should be recognized and amortized over the calendar year.

.250 The HCERA contains a number of provisions that will affect the accounting for many entities. This issue addresses one aspect of accounting for the fees payable by pharmaceutical manufacturers to the federal government. The HCERA imposes an annual fee on the pharmaceutical manufacturing sector for each calendar year beginning after 2010. The fee ranges from $2.5 billion to $4.1 billion and is payable by no later than September 30 of the applicable calendar year. This is a nondeductible fee that will be allocated across the industry based on relative market share. The annual fee payable in a given calendar year is determined by reference to sales in the preceding calendar year. This issue applies to all pharmaceutical manufacturers that are subject to this fee, which according to Section 9008 of the HCERA is any manufacturer or importer with gross receipts from branded prescription drug sales to any federal government program. Practice is likely to recognize the fee in earnings on a ratable basis in the calendar year in which the fee is paid. The rationale is that a pharmaceutical company does not have a liability, as defined by FASB Concepts Statement No. 6, *Elements of Financial Statements—a replacement of FASB Concepts*

Statement No. 3 (incorporating an amendment of FASB Concepts Statement No. 2), prior to the year sales are made that trigger the payment.

.251 Although there does not appear to be diversity in the timing of when the fees will be recognized, divergent views do exist about how such fees should be classified in the income statement. Some constituents believe that the fees should be classified as a reduction of revenue, but others believe they should be accounted for as an operating cost.

.252 The amendments in the proposed ASU specify that upon recognition of the liability, the annual fee would be (*a*) recognized over the calendar year that it is payable using a straight-line method of allocation, unless another method better allocates the fee over the calendar year it is payable, and (*b*) presented as operating expenses.

.253 The amendments in the proposed ASU would be effective for calendar years beginning after December 31, 2010, when the fee initially becomes effective. Readers should be alert to the final issuance of this ASU.

Accounting for Legal Costs Associated With Medical Malpractice Claims *Exposure Draft*

.254 In August 2010, FASB issued a proposed ASU on accounting for legal costs associated with medical malpractice claims. The main issue of this proposal is whether the industry-specific requirement that health care entities accrue legal costs related to litigating medical malpractice claims or similar claims before those costs are incurred should be eliminated.

.255 In other industries, entities make an accounting policy election to either expense legal fees as incurred or accrue estimated legal fees when the associated claim is incurred (FASB ASC 450-20-S99-2). Some believe that guidance would benefit from eliminating an industry-specific exception for health care entities and aligning the accounting practices in that industry with FASB ASC 450-20.

.256 The objective of the proposed ASU is to eliminate the industry-specific requirement that health care entities accrue legal costs related to litigating medical malpractice claims or similar claims before these costs are incurred.

.257 The amendment would affect health care entities within the scope of FASB ASC 954, *Health Care Entities*. The amendment would allow health care entities to make a policy election to expense legal fees as incurred or accrue estimated legal fees when the associated claim is incurred. The effective dates of this proposed amendment would be determined after the feedback from the draft is considered. However, the amendments would be applied retrospectively to all prior periods presented. Readers should be alert to the final issuance of this ASU.

Disclosure of Certain Loss Contingencies

.258 In July 2010, FASB issued an exposure draft on the disclosure of certain loss contingencies in response to concerns from investors and other financial statement users that the current disclosures do not provide adequate and timely information to assess the likelihood, timing, and magnitude of future cash outflows associated with loss contingencies. The objective of these disclosures would be for an entity to disclose qualitative and quantitative information about loss contingencies to enable financial statement users to understand all of the following: the nature of the loss contingencies, their potential magnitude, and their potential timing (if known). Disclosure of certain remote loss contingencies would be required and, therefore, would expand the population of loss contingencies that are required to be disclosed. An entity would not consider the possibility of recoveries from insurance or other indemnification arrangements when assessing the materiality of loss contingencies to determine whether disclosure is required. Further, current qualitative disclosures would be enhanced by requiring additional disclosures. These additional required qualitative and quantitative disclosures include the following:

- For litigation contingencies, the contentions of the parties and how users can obtain more information about the litigation
- Publicly available quantitative information, such as the claim amount for asserted litigation contingencies; other relevant non-privileged information; and, in some cases, information about possible recoveries from insurance and other sources
- For public entities, tabular reconciliations, by class, of recognized (accrued) loss contingencies that present the activity in the account during the period

.259 The amendments in this proposal would affect all entities. The exposure draft noted that FASB will continue to work with the PCAOB, the AICPA, and the American Bar Association (ABA) to identify and address any potential implications of the proposed amendments for auditing literature and the ABA's Statement of Policy Regarding Lawyers' Responses to Auditors' Requests for Information. The proposed amendments would be effective for fiscal years ending after December 15, 2010, for public entities and in the first annual period beginning after December 15, 2010, for nonpublic entities. The comment period ended in September 2010.

Going Concern FASB Project

.260 Currently, the only guidance on going concern resides in the auditing literature, and this project's intention is to incorporate going concern guidance into U.S. GAAP. Specifically, this guidance would discuss the following:

- Preparation of financial statements as a going concern
- An entity's responsibility to evaluate its ability to continue as a going concern
- Disclosure requirements when financial statements are not prepared on a going concern basis
- Disclosure requirements when there is a substantial doubt about an entity's ability to continue as a going concern
- The adoption and application of the liquidation basis of accounting

.261 A revised exposure draft is expected to be issued in the second quarter of 2010, with a final ASU expected in the third quarter of 2010. FASB has decided that management should take into account available information about the foreseeable future, which is generally, but not limited to, 12 months from the end of the reporting period. Readers should be alert to developments on this topic.

Other Accounting Projects

.262 Additionally, FASB has the following projects underway:

- Troubled debt restructuring
- Disclosure framework
- Investment properties

Resource Central

.263 The following are various resources that practitioners engaged in the health care industry may find beneficial.

Publications

.264 Practitioners may find the following publications useful. Choose the format best for you—online or print.

- Audit and Accounting Guide *Health Care Entities* (2010) (product no. 0126110 [paperback] or WHC-XX [online with the associated Audit Risk Alert])
- Audit and Accounting Guide *Not-for-Profit Entities* (2010) (product no. 0126410 [paperback], WNP-XX [online with the associated Audit Risk Alert])
- Audit Guide Government Auditing Standards *and Circular A-133 Audits* (2010) (product no. 0127410 [paperback], WRF-XX [online with associated Audit Risk Alert])
- Audit and Accounting Guide *State and Local Governments* (2010) (product no. 0126610 [paperback]. WGG-XX [online with the associated Audit Risk Alert])
- Audit Guide *Analytical Procedures* (2008) (product no. 012558 [paperback] or WAN-XX [online])
- Audit Guide *Assessing and Responding to Audit Risk in a Financial Statement Audit* (2009) (product no. 012459 [paperback] or WRA-XX [online])
- Audit Guide *Auditing Derivative Instruments, Hedging Activities, and Investments in Securities* (2010) (product no. 0125210 [paperback] or WDI-XX [online])
- Guide *Compilation and Review Engagements* (2010) (product no. 0128110 [paperback] or WRC-XX [online])
- Audit Guide *Auditing Revenue in Certain Industries* (2010) (product no. 0125110 [paperback] or WAR-XX [online])
- Audit Guide *Audit Sampling* (2008) (product no. 012538 [paperback] or WAS-XX [online])
- Compilation and Review Alert *Compilation and Review Developments—2010/11* (product no. 0223010 [paperback])
- Audit Risk Alert *General Accounting and Auditing Developments—2010/11* (product no. 0223310 [paperback] or WGE-XX [online])
- Audit Risk Alert *Independence and Ethics Developments—2010/11* (product no. 0224710 [paperback] or WIA-XX [online])

- Checklists and Illustrative Financial Statements *Health Care Entities* (product no. 0090210 [paperback] or WHE-CL [online])
- *Accounting Trends & Techniques, 62nd Edition* (product no. 0099009 [paperback] or WAT-XX [online])
- *IFRS Accounting Trends & Techniques* (product no. 0099109 [paperback] or WIF-XX [online])
- *Audit and Accounting Manual* (2010) (product no. 0051310 [paperback], WAM-XX [online], or AAM-XX [loose leaf])

AICPA Online Professional Library: Accounting and Auditing Literature

.265 The AICPA has created your core accounting and auditing library online. The AICPA Online Professional Library is now customizable to suit your preferences or your firm's needs. Or, you can sign up for access to the entire library. Get access—anytime, anywhere—to FASB ASC, the AICPA's latest *Professional Standards*, *Technical Practice Aids*, Audit and Accounting Guides, Audit Risk Alerts, *Accounting Trends & Techniques*, and more. One option is the *AICPA Audit and Accounting Guides with FASB* Accounting Standards Codification™, which contains all audit and accounting guides, all audit risk alerts, and FASB ASC in the Online Professional Library (product no. WFA-XX [online]).To subscribe to this essential online service for accounting professionals, visit www.cpa2biz.com.

Continuing Professional Education

.266 The AICPA offers a number of continuing professional education (CPE) courses that are valuable to CPAs working in public practice and industry, including the following:

- *AICPA's Annual Accounting and Auditing Update Workshop (2010–2011 Edition)* (product no. 730096 [text] or 180096 [DVD]). Whether you are in industry or public practice, this course keeps you current and informed and shows you how to apply the most recent standards.
- *Internal Control Essentials for Financial Managers, Accountants and Auditors* (product no. 731856 [text], 181856 [DVD/Manual], or 351856 [Additional Manual for DVD]). This course will provide you with a solid understanding of systems and control documentation at the significant process level.
- *International Versus U.S. Accounting: What in the World is the Difference?* (product no. 731668 [text] or 181661 [DVD]). Understanding the differences between IFRSs and U.S. GAAP is becoming more important for businesses of all sizes. This course outlines the major differences between IFRSs and U.S. GAAP.
- *IFRS Essentials with GAAP Comparison: Building a Strong Foundation* (product no. 741602 [text], 181601 [DVD/Manual], or 351601 [Additional Manual for DVD]). This course provides you with a greater understanding of what you need to know as the acceptance of international standards continues to grow.

.267 Visit www.cpa2biz.com for a complete list of CPE courses.

Online CPE

.268 AICPA CPExpress, offered exclusively through CPA2Biz, is the AICPA's flagship online learning product. AICPA members pay $180 for a new subscription and $145 for the annual renewal. Nonmembers pay $435 for a new subscription and $375 for the annual renewal. Divided into 1-credit and 2-credit courses that are available 24 hours a day, 7 days a week, AICPA CPExpress offers hundreds of hours of learning in a wide variety of topics. Some topics of special interest to the health care industry include the following:

- *Nonprofit Auditing: Unique Auditing for a Unique Entity*
- *Fraud in Exempt Organizations: The Governmental and Not-for-Profit Environments*
- *Nonprofit Accounting: Financial Reporting*
- *Auditing Considerations in an Uncertain Economy*

.269 To register or learn more, visit www.cpa2biz.com.

Webcasts

.270 Stay plugged in to what is happening and earn CPE credit right from your desktop. AICPA webcasts are high quality, two-hour CPE programs that bring you the latest topics from the profession's leading experts. Broadcast live, they allow you to interact with the presenters and join in the discussion. If you cannot make the live event, each webcast is archived and available on CD-ROM. For additional details on available webcasts, please visit www.cpa2biz.com/AST/AICPA_CPA2BIZ_Browse/Store/Webcasts.jsp.

Member Service Center

.271 To order AICPA products, receive information about AICPA activities, and get help with your membership questions, call the AICPA Service Operations Center at (888) 777-7077.

Hotlines

Accounting and Auditing Technical Hotline

.272 Do you have a complex technical question about GAAP, other comprehensive bases of accounting, or other technical matters? If so, use the AICPA's Accounting and Auditing Technical Hotline. AICPA staff will research your question and call you back with the answer. The hotline is available from 9 a.m. to 8 p.m. EST on weekdays. You can reach the Technical Hotline at (877) 242-7212 or online at www.aicpa.org/Research/TechnicalHotline/Pages/TechnicalHotline.aspx. Members can also e-mail questions to aahotline@aicpa.org. Additionally, members can submit questions by completing a Technical Inquiry form found on the same website.

Ethics Hotline

.273 In addition to the Technical Hotline, the AICPA also offers an Ethics Hotline. Members of the AICPA's Professional Ethics Team answer inquiries concerning independence and other behavioral issues related to the application of the AICPA Code of Professional Conduct. You can reach the Ethics Hotline at (888) 777-7077 or by e-mail at ethics@aicpa.org.

Industry Conference

.274 The AICPA offers an annual health care industry conference in the fall. The health care industry conference is a two-day conference designed to update attendees on recent developments related to the health care industry. The AICPA National Health Care Industry Conference will be held on Nov 11–12, 2010, in Las Vegas, NV. For further information about the conference, call (888) 777-7077 or visit www.cpa2biz.com.

AICPA Governmental Audit Quality Center

.275 The Governmental Audit Quality Center (GAQC) is firm-based, voluntary membership center designed to improve the quality and value of governmental audits provided to purchasers of governmental audit services. Governmental audits are performed under *Government Auditing Standards* and are audits and attestation engagements of federal, state, or local governments; NFP organizations; and certain for-profit organizations, such as housing projects and colleges and universities that participate in governmental programs or receive governmental financial assistance. The GAQC keeps member firms informed about the latest developments and provides them with tools and information to help them better manage their audit practice. Firms and that join demonstrate their commitment to audit quality by agreeing to adhere to certain membership requirements.

.276 The GAQC has been in existence since September 2004. Since its launch, center membership has grown to almost 1400 firms from 50 states, the District of Columbia, Puerto Rico, and the U.S. Virgin Islands. The membership accounts for approximately 84 percent of the total federal expenditures covered in single audits performed by CPA firms in the Federal Audit Clearinghouse database (http://harvester.census.gov/sac/) for the year 2009.

.277 The GAQC's focus is to promote the highest quality audits and to save firms time by providing a centralized place to find information that they need, when they need it, to maximize quality and practice success. Center resources include the following:

- E-mail alerts with the latest audit and regulatory developments, including information on the Recovery Act and its impact on your audits
- Exclusive web seminars, webcasts, and teleconferences on compliance auditing and timely topics relevant to governmental and NFP financial statement audits (optional CPE is available for a small fee, and events are archived online)
- Dedicated GAQC website at www.aicpa.org/InterestAreas/GovernmentalAuditQuality/Pages/GAQC.aspx with resources (including a Recovery Act Resource Center), community events, and products, and a complete listing of GAQC members in each state
- Online member discussion forums for sharing best practices and discussing issues firms are facing
- Savings on professional liability insurance

.278 For more information about the GAQC, visit www.aicpa.org/InterestAreas/GovernmentalAuditQuality/Pages/GAQC.aspx.

The Center for Audit Quality

.279 The Center for Audit Quality (CAQ), which is affiliated with the AICPA, was created to serve investors, public company auditors, and the markets. The CAQ's mission is to foster confidence in the audit process and aid investors and the capital markets by advancing constructive suggestions for change rooted in the profession's core values of integrity, objectivity, honesty, and trust.

.280 To accomplish this mission, the CAQ works to make public company audits even more reliable and relevant for investors in a time of growing financial complexity and market globalization. The CAQ also undertakes research, offers recommendations to enhance investor confidence and the vitality of the capital markets, issues technical support for public company auditing professionals, and helps facilitate the public discussion about modernizing business reporting. The CAQ is a voluntary membership center that provides education, communication, representation, and other means to member firms that audit or are interested in auditing public companies. To learn more about the CAQ, visit www.aicpa.org/InterestAreas/CenterForAuditQuality/Pages/CAQ.aspx.

AICPA Industry Expert Panel—Health Care

.281 For information about the activities of the AICPA Health Care Expert Panel, visit the panel's website at www.aicpa.org/INTERESTAREAS/ACCOUNTINGANDAUDITING/COMMUNITY/HEALTHCARE/Pages/Healthcare.aspx.

Industry Websites

.282 The Internet covers a vast amount of information that may be valuable to auditors of health care entities, including current industry trends and developments. Some of the more relevant sites for auditors with health care industry clients include those shown in the following table:

Organization	***Website***
Centers for Medicare & Medicaid Services	www.cms.hhs.gov
U.S. Department of Health & Human Services	www.hhs.gov
Global health reporting	http://globalhealth.kff.org/
Kaiser Family Foundation	www.kff.org
Atlantic Information Services	www.aishealth.com

.283 The health care practices of some of the larger CPA firms also may contain industry-specific auditing and accounting information that is helpful to auditors.

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Appendix—Additional Internet Resources

Here are some useful websites that may provide valuable information to accountants.

Website Name	*Content*	*Website*
AICPA	Summaries of recent auditing and other professional standards, as well as other AICPA activities	www.aicpa.org www.cpa2biz.com www.ifrs.com
AICPA Financial Reporting Executive Committee (formerly known as Accounting Standards Executive Committee [AcSEC])	Summaries of recently issued guides, technical questions and answers, and practice bulletins containing financial, accounting, and reporting recommendations, among other things	www.aicpa.org/InterestAreas/AccountingAndAuditing/Community/FINREC/Pages/FinREC.aspx
AICPA Accounting and Review Services Committee	Summaries of review and compilation standards and interpretations	www.aicpa.org/InterestAreas/AccountingAndAuditing/Community/AccountingReviewServicesCommittee/Pages/ARSC.aspx
AICPA Professional Issues Task Force	Summaries of practice issues that appear to present concerns for practitioners and disseminate information or guidance, as appropriate, in the form of practice alerts	www.aicpa.org/InterestAreas/AccountingAndAuditing/Resources/AudAttest/AudAttestGuidance/Pages/PITFPracticeAlerts.aspx
Economy.com	Source for analyses, data, forecasts, and information on the U.S. and world economies	www.economy.com
The Federal Reserve Board	Source of key interest rates	www.federalreserve.gov
Financial Accounting Standards Board (FASB)	Summaries of recent accounting pronouncements and other FASB activities	www.fasb.org

Website Name	***Content***	***Website***
USA.gov	Portal through which all government agencies can be accessed	www.usa.gov
Government Accountability Office	Policy and guidance materials and reports on federal agency major rules	www.gao.gov
Governmental Accounting Standards Board (GASB)	Summaries of recent accounting pronouncements and other GASB activities	www.gasb.org
International Accounting Standards Board	Summaries of International Financial Reporting Standards and International Accounting Standards	www.iasb.org
International Auditing and Assurance Standards Board	Summaries of International Standards on Auditing	www.iaasb.org
International Federation of Accountants	Information on standards setting activities in the international arena	www.ifac.org
Private Company Financial Reporting Committee	Information on the initiative to further improve FASB's standard setting process to consider needs of private companies and their constituents of financial reporting	www.pcfr.org
Public Company Accounting Oversight Board (PCAOB)	Information on accounting and auditing activities of the PCAOB and other matters	www.pcaob.org
Securities and Exchange Commission (SEC)	Information on current SEC rulemaking and the Electronic Data Gathering, Analysis, and Retrieval database	www.sec.gov